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HELPING HOMEOWNERS HARMED BY FORECLOSURES: ENSURING ACCOUNTABILITY AND TRANSPARENCY IN FORECLOSURE REVIEWS—PART II

HEARING

BEFORE THE

SUBCOMMITTEE ON
HOUSING, TRANSPORTATION, AND COMMUNITY DEVELOPMENT

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDRED THIRTEENTH CONGRESS

FIRST SESSION

ON

EXAMINING THE EFFORTS TO ENHANCE TRANSPARENCY, ACCOUNTABILITY, AND CONSISTENCY IN BOTH THE INDEPENDENT FORECLOSURE REVIEW AND NATIONAL MORTGAGE SETTLEMENT

APRIL 17, 2013

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C O N T E N T S

WEDNESDAY, APRIL 17, 2013

HELPING HOMEOWNERS HARMED BY FORECLOSURES: ENSURING ACCOUNTABILITY AND TRANSPARENCY IN FORECLOSURE REVIEWS—PART II

WEDNESDAY, APRIL 17, 2013

U.S. SENATE,
SUBCOMMITTEE ON HOUSING, TRANSPORTATION, AND COMMUNITY DEVELOPMENT,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Subcommittee convened at 10:05 a.m., in room SD–538, Dirksen Senate Office Building, Hon. Robert Menendez, Chairman of the Subcommittee, presiding.

OPENING STATEMENT OF CHAIRMAN ROBERT MENENDEZ

Chairman MENENDEZ. Good morning. This hearing of the Subcommittee on Housing, Transportation, and Community Development will come to order. Let me thank you all for being here. I know that Senator Moran, the Ranking Member, will be here in short order.

Today's hearing is about "Helping Homeowners Harmed by Foreclosures and Ensuring Accountability and Transparency in Foreclosure Reviews." This issue is important to every homeowner, especially those harmed by illegal foreclosure practices. It is of particular concern to countless New Jerseyans who have contacted my office, almost all with heartwrenching stories about their experiences going through the foreclosure process, stories in many cases of being either mistreated, neglected, and in some cases insulted and embarrassed by their mortgage servicers.

In response to illegal foreclosure practices, regulators and the Nation's five largest servicers announced a National Mortgage Settlement in February of 2012. As part of the settlement, servicers are to provide about $25 billion of relief to homeowners and individuals who were victims of such illegal practices.

The Federal Reserve Board and the Office of the Comptroller of the Currency also announced the Independent Foreclosure Review process with 14 mortgage servicers. The goal of the IFR was to identify as many harmed borrowers as possible, to treat similarly situated borrowers across all 14 services in a consistent manner, and to help restore public confidence in the mortgage market. But challenges and the complexity of the IFR prevailed and regulators and 13 of the mortgage servicers abandoned the IFR process in

January of this year and instead agreed to a new framework that would no longer evaluate each mortgage for actual harm.

As we attempt to correct these past illegal foreclosures, we must have transparency, consistency, and accountability. After being hard hit by the foreclosure crisis and other economic woes, American homeowners expect and deserve confidence in the mortgage market, and it is our job to give them that confidence.

First, we must learn from the mistakes of the past, remain committed to not repeating them in the future. So I asked the Government Accountability Office to conduct a study on the IFR, focusing on challenges to the achievement of the goals of the reviews, transparency of the process, and lessons that could be learned moving forward.

It has been nearly 2 years since the Consent Orders were signed, and in that time, over a billion dollars went to third party consultants. But affected borrowers received nothing, even when there was documented evidence of bad practices. There is certainly plenty of blame to go around, but the American people will not accept excuses for the failures of our regulators. They expect our regulators to be up to the task, fully capable of overcoming the challenges of these settlements, and effective oversight of our financial system should be the number one priority.

Over 4.5 million people were potentially impacted by these illegal foreclosure abuses and they deserve our best efforts and attention. The time to act is now, and that is why we are here today, to get to the bottom of some of these important issues.

So let me, in the absence of any Member at this point to be here, let me start introducing our panel. Mr. Lawrance Evans is the Director of Financial Markets and Community Investment at the Government Accountability Office. He directs a body of work in the area of banking and financial intermediation, including leading efforts on the GAO study of the Independent Foreclosure Review. In his prior role as a Lead eConomist, he managed a diverse portfolio at GAO which included engagements on TARP, Dodd-Frank's bank capital provisions, and Sarbanes-Oxley. So we thank you for your work and we look forward to your testimony.

Mr. Joseph Smith is the Monitor of the National Mortgage Settlement, which was announced in February of 2012 by 49 State Attorneys General and the Federal Government to provide $25 billion in relief for distressed borrowers.

Mr. David Holland is the Executive Vice President of Rust Consulting, Incorporated, a contractor that does outreach to homeowners for the foreclosure reviews and is administering the payments for the amended Consent Agreement for the IFR.

And Ms. Deborah Goldberg is the Special Project Director at the National Fair Housing Alliance, where she advocates before Congress and Federal regulatory agencies on predatory lending and sustainable home ownership issues.

So, let me thank you all for appearing today. We look forward to getting your perspective on the situation and your view on the approach moving forward. I am going to ask each of you, in the order that I introduced you, to synthesize your statement for about 5 minutes or so. Without objection, all of your entire statements will be entered into the record, and then we look forward to having a conversation with you.

Mr. Evans.

STATEMENT OF LAWRANCE L. EVANS, JR., DIRECTOR, FINANCIAL MARKETS AND COMMUNITY INVESTMENT, GOVERNMENT ACCOUNTABILITY OFFICE

Mr. EVANS. Thank you. Chairman Menendez, I am pleased to be here this morning to discuss GAO's ongoing assessment of the Independent Foreclosure Review. My remarks today are based on our March 2013 report, developed in response to the amended Consent Orders that replaced the IFR for most servicers with a broader framework that will provide cash payments to all eligible borrowers.

The IFR was intended to identify as many harmed borrowers as possible, to ensure consistent treatment and to help restore public confidence in the mortgage market. Our report highlighted issues stemming from insufficient planning, monitoring, and communication that impeded the regulators' ability to achieve the stated goals. I will briefly review our key findings, including lessons learned, which, if leveraged properly, can lead to better outcomes for the ongoing reviews and activities under the payment agreements.

First, it is important to note that the IFR was, indeed, unprecedented, and the size and scope of the operation posed significant challenges to regulators. There were 4.3 million eligible borrowers across 14 different servicers, seven consultants, and ten law firms. The foreclosure files themselves were sizable and touched on a large number of complex issues, ranging from State and Federal laws to Loan Modification Program guidelines. In testimony before the Senate law week, both OCC and the Federal Reserve noted that they underestimated the scale, scope, and complexity of the reviews.

Second, while some issues were inevitable, these challenges were exacerbated by overly broad guidance and limited monitoring for the consistency and sufficiency of the consultants' review activities. For example, lack of clarity in sampling guidance resulted in variations in methodologies used by consultants which would have limited the ability of regulators to aggregate the results and pull together a statistically valid description of the extent of errors in foreclosure processing. Moreover, the guidance did not include mechanisms to facilitate oversight of the extent to which consultants would have identified as many harmed borrowers as possible or targeted the appropriate high-risk categories.

In general, these issues limited the types of information regulators could know and report and increased the risk of inconsistent results for similarly situated borrowers. Overall, regulators missed opportunities to develop common criteria or reference documents to help consultants navigate complexities involving State foreclosure law and loss mitigation activities, among other issues. In absence of such guidance, consultants developed their own test questions to determine harm and potential remediation, again, raising the risk of inconsistent treatment.

Third, the absence of timely and useful communication at certain stages of the process undermined public confidence in the reviews.

Although regulators released more information that is typically associated with Consent Orders, borrowers and the general public received limited information about the status of the reviews. Also, some stakeholders perceived informational gaps that raised concerns about how the reviews were being executed and the process for determining error and remediation.

Last, several issues emerged as lessons learned for regulators. Most notably, we observed that advance planning can enhance project design and better ensure the achievement of goals. Important here is appropriate consultation with stakeholders and establishing mechanisms to systematically monitor progress toward goals. Consultation with organizations directly responsible for, or familiar with, particular aspects of the review before initiating the IFR may have allowed regulators to define the scope of activities more appropriately and issue more complete guidance. Had regulators incorporated monitoring mechanisms into the design, they would have been better equipped to produce reliable and relevant data for oversight and management. In the absence of systematic processes to monitor activities, regulators did not have an early warning mechanism to help identify problem areas.

While the goals of the IFR were hampered, it is possible that the regulators could have taken steps to address some of these issues. In fact, regulators took a number of steps during the process to foster consistency. However, such actions are second best to up-front planning, as they increase the risk of further delays, rework, including the retraining of reviewers.

The final lesson learned is that transparency is essential for public confidence, and advance planning should give consideration to the types of data required to credibly communicate useful information to the intended audience. Unfortunately, the regulators are limited in what they can report because they did not plan for reporting in the design of the reviews.

Based on these findings, we offered three recommendations to the regulators aimed at using lessons learned to improve outcomes for the ongoing reviews and activities under the amended Consent Orders. Both OCC and the Federal Reserve were receptive to all three.

Chairman Menendez and Members of the Subcommittee, this concludes my prepared statement. I will be happy to answer any questions you may have.

Chairman MENENDEZ. Thank you.

Mr. Smith.

STATEMENT OF JOSEPH A. SMITH, JR., MONITOR OF THE NATIONAL MORTGAGE SETTLEMENT

Mr. SMITH. Chairman Menendez, Senator Merkley, good morning. Thank you for inviting me to testify about the implementation of the National Mortgage Settlement.

In April 2012, the National Mortgage Settlement went into effect when the United States District Court for the District of Columbia entered five separate consent judgments that settled claims of improper mortgage servicing practices against five major mortgage servicing organizations, Bank of America, Citi, Chase, the ResCap parties, which are the former GMAC, and Wells Fargo. Government parties to the settlement included the Departments of HUD and Justice, Attorneys General from 49 States and the District of Columbia, various State financial services regulatory agencies, and other releasing parties, including the CFPB and Treasury.

The settlement can be divided into three parts: Direct payments to borrowers and States, consumer relief, and servicing standards. While I have no oversight over the direct payments, I am responsible for reviewing and certifying the discharge of the servicers' consumer relief obligations and monitoring implementation of the servicing standards. I am subject to oversight by a monitoring committee that is comprised of representatives of the Departments of HUD and Justice and representatives of 15 States.

Under the settlement, the servicers have agreed to provide specific dollar amounts of relief to distressed borrowers within a 3-year period. In February, the servicers reported that during 2012, 550,000 borrowers benefited from some type of consumer relief, totaling $46 billion, which, on average, represents about $83,000 per borrower. The kinds of consumer relief for which a servicer can receive credit under the settlement are set out in detail in the consent judgments, and the credit varies based on the relief given. For that reason, the gross dollar amounts of relief the servicers reported far exceeds the total credited obligations under the settlement.

To date, only the ResCap parties have requested a determination that they have completed their consumer relief obligations. In February of this year, after a review of their performance, I issued a report to the court that they had satisfied their minimum consumer relief obligations and partially satisfied their mandatory solicitation obligations under the settlement.

In addition to consumer relief, the settlement establishes 304 servicing standards, or rules of conduct, to which the servicers must adhere. Each servicer has been responsible for compliance with the standards since October of 2012. There are servicing standards related to document integrity, the loan modification process, dual tracking, single points of contact, and other customer service and more general requirements.

Under the settlement, I measure servicer compliance with the servicing standards through 29 metrics, or tests. The servicers conduct these tests internally and report the results to me. Assisted by independent professionals in my employ, I assess the work of servicers and report my conclusions. If the Internal Review Groups or I find noncompliance with the standards, the servicer has to implement a corrective action plan and, in the case of widespread error, to remediate. If it cannot or will not correct the potential violations, injunctions or civil penalties can be sought through the United States District Court for the District of Columbia.

My independent professionals and I are nearing completion of our reviews of servicer compliance with the metrics through year-end 2012 and intend to issue our report on it to the court and the public next month. Our work will continue over the next 2 years.

To help me better understand the settlement's impact in the marketplace, my colleagues and I closely review complaints we receive through my office as well as the complaints elected officials submit to the banks. I also have met with the Attorneys General, consumers, and professionals who represent them in a number of hard-hit States. As a result of what I have heard from consumers and professionals, I am now working with the banks to establish additional metrics to address what I have learned.

In closing, the settlement has been successful in what I believe is a worthwhile effort, focusing resources on a specific problem in a targeted, time-limited way that augments and supports the work of policy makers and Government agencies. I look forward to continuing my work toward that goal and I welcome your questions.

Thank you very much, Senators.

Chairman MENENDEZ. Thank you.

Mr. Holland.

STATEMENT OF DAVID HOLLAND, EXECUTIVE VICE PRESIDENT, RUST CONSULTING

Mr. HOLLAND. Senator, or Chairman Menendez, Senator Merkley, thank you for the opportunity to appear today on behalf of Rust Consulting.

Rust Consulting has been engaged by the servicers to administer certain aspects of the Alternative Resolution Settlement, as directed by the Office of the Comptroller of the Currency and the Federal Reserve Board. Previously, Rust was engaged by the servicers to administer the Consent Orders for the Independent Mortgage Foreclosure Borrower Outreach Project, also known as the Independent Foreclosure Review or IFR.

Under the IFR Consent Orders, our responsibilities were to notify homeowners about the program, to answer their questions, to review their requests for review forms, and to handle in- and outbound mail. From November 2011 through December 2012, we executed three mass mailings to homeowners along with a series of media notice campaigns. Over the same period and through January 2013, we received completed requests for review forms and forwarded them to the servicers.

We were recently engaged by 11 of the 14 original servicers, along with two additional servicers, to serve as a paying agent under the Alternative Resolution Settlement. Our responsibilities under the settlement are to notify homeowners about the program, answer their questions, and distribute settlement payments in the form of checks to eligible homeowners.

Rust mailed postcards on March 18, 2013, informing eligible homeowners that they were to receive a payment as a result of the settlement. Also, we received relevant settlement data from servicers that identified loan classifications for each individual loan, and subsequently received data from the OCC and FRB detailing the payment amounts for each loan classification.

The first wave of checks were mailed on Friday, April 12. Yesterday, we became aware of check cashing issues that some payees encountered and we are addressing those issues and will have solutions in place today and on a go-forward basis. The majority of the remaining checks will be mailed in three more waves occurring on April 19, April 26, and May 3.

Rust continues to staff a call center to take incoming calls from homeowners with questions about the program. We also updated the IFR Web site to provide new information regarding the settlement.

At the direction of the servicers, the OCC, and the FRB, Rust implemented a number of address correction processes in order to maximize the number of homeowners who receive notice as part of the IFR. Rust will continue to use address correction processes under the settlement. In both projects, the National Change of Address process was used to update addresses. And as part of the IFR, Rust received "undeliverable" notices, ran the corresponding addresses through a "skip-trace" program, and remailed notices to new addresses. For any of the remailed notices that were returned as undeliverable a second time, Rust performed another second type of address search and again remailed notices to new addresses.

Under the settlement, Rust will receive undeliverable checks, attempt to find better addresses, and remail checks to new addresses.

During the IFR process, Rust provided comprehensive daily statistical reporting to the OCC, the FRB, independent consultants, and the servicers. Daily meetings were held with a consortium of the 14 servicers and independent consultants that covered the current state of project execution, future deliverables, and next phase planning.

As part of the settlement, Rust provides comprehensive daily statistical reporting to the OCC, the FRB, and the servicers. Daily conference calls are held with the servicers covering project execution. Two times weekly, conference calls are held with the OCC and the FRB covering project execution and future deliverables.

Thank you. I would be happy to answer your questions.

Chairman MENENDEZ. Thank you.

Ms. Goldberg.

STATEMENT OF DEBORAH GOLDBERG, SPECIAL PROJECT DIRECTOR, NATIONAL FAIR HOUSING ALLIANCE

Ms. GOLDBERG. Thank you, Mr. Chairman. Mr. Chairman and Senator Merkley, thank you for inviting me here today to testify, and thank you, too, for your engagement in this issue. You have brought much needed attention and oversight to the Independent Foreclosure Review process.

The IFR is the only real Federal effort to identify and compensate borrowers who were harmed by their mortgage servicers when their loans became unsustainable and they needed help to save their homes. While this and other programs seek to prevent future foreclosures, the IFR stands alone as an effort to begin to make borrowers whole. This is significant because of the harm caused by the foreclosure crisis.

While foreclosures have affected virtually every community, certain communities have suffered more than others. During the heyday of subprime lending, communities of color were flooded with unsustainable subprime loans. Borrowers who should have gotten safer, cheaper prime loans were given subprime loans because they were more profitable. This happened to borrowers of color much more often than to white borrowers. Not surprisingly, these borrowers have suffered much higher rates of foreclosure and they and their neighbors have lost tremendous wealth as a result.

We hoped the IFR would begin to set things right, but from the beginning, it has been plagued with a lack of transparency and accountability that has undermined its success. It has failed to identify borrowers who suffered harm and in doing so to shed light on the nature and extent of the problems in the mortgage servicing industry. It has not provided adequate compensation to borrowers, and to date, it has failed to bring about the kind of servicing reforms that are needed to prevent future unnecessary foreclosures.

With the announcement of the new settlement in January, the IFR game has changed. With the rest of my time, I would like to highlight some concerns with the settlement's $5.7 billion worth of noncash assistance and some ways in which the regulators can increase the positive impact of their Consent Orders.

So this so-called soft dollar side of the IFR agreement is similar to the structure of the National Mortgage Settlement, or NMS. Unfortunately, the particulars differ from the NMS in three key ways that severely deflate the value and limit the impact of these soft dollars.

First, it fails to make saving homes a priority. It places loan modifications, which can save homes, on an equal footing with short sales and deeds-in-lieu, which do not.

Second, it gives the servicers credit based not on the amount of loan principal they forgive, but on the unpaid balance of the loan. This creates an incentive to modify loans with large balances because that is the fastest way for the servicers to get the most credit. It will likely mean that many fewer loans are modified than could have been the case.

And third, this approach places borrowers of color and low- and moderate-income borrowers at a disadvantage because they tend to live in communities where home values and loan balances are smaller. Modifying their loans will put the servicers on a slower road to meeting their soft dollar goals.

We are very disappointed that the settlement was structured this way and we are concerned that many homes that could have been saved from foreclosure will be lost. However, there are two areas in which we believe the regulators can still make a positive impact in implementation of the IFR Settlement.

The first is the area of transparency. We had asked the regulators to make public detailed information about who is getting help as a result of this settlement, both through the direct cash payments and the noncash assistance. These data must be broken out by servicer and by census tract so that the public can see whether the communities that have suffered the most are getting the assistance they need and deserve. The timely release of such information will help to hold the servicers accountable. It is also necessary to begin to rebuild public confidence in our regulatory system.

The second is the area of oversight. Despite all of the servicing rules that have been written and all of the scrutiny to which servicers have been subject, mortgage servicing abuses remain all too common. They must be brought to an end so that the millions of homeowners still at risk of foreclosure can get the help they are supposed to get to save their homes. By stepping up their oversight and enforcement, the regulators can help accomplish this goal.

Recently, the regulators have shown some interest in exploring these recommendations. I am hopeful that they will do so and that they will put them into action. But as long as problems persist in the mortgage servicing industry, we need you in Congress to keep up the pressure and continue your oversight. There are still some gaps in the servicing rules that must be closed, such as protections for people with limited proficiency in English, borrowers with disabilities, and the widows and heirs of deceased homeowners who cannot get help from their servicers. We look forward to working with you and the regulators to address these problems.

Thank you again for the opportunity to testify today. I look forward to your questions.

Chairman MERKLEY. Well, thank you all very much, and we will start with a round of questions.

Mr. Evans, the report by the Government Accountability Office found the following things. Correct me if I am wrong in any of them.

Mr. EVANS. OK.

Chairman MENENDEZ. The goals of IFR to identify as many harmed borrowers as possible and ensure similar results for similar borrowers were not met.

The regulator guidance did not specify key sampling parameters to consultants for file review, resulting in delays and difficulty assessing borrower harm.

Limited communication with borrowers and the public adversely impacted transparency and public confidence.

Regulators considerably see more data, but express concerns that doing so might disclose private information.

Borrowers face significant gaps in promised review documentation from regulators and consultants, with some waiting over a year.

No standard sampling method or process between servicers or other independent consultants led to reduced reliability of data.

Regulators stopped the IFR process without having a sufficient and objective method—a sufficient and objective method—to determine if the proper number of reviews had been sampled to uncover borrowers harmed.

Limited regulator monitoring and inconsistencies in consulting methodology increased the risk of treating borrowers with similar types of harm differently.

And regulators did not rely on stakeholder consultation enough, such as housing counselors, community groups with expertise in loss mitigation and loan modifications.

Is that an accurate synthesis of the GAO report?

Mr. EVANS. I think so, in general. There are just a few technical notes I will make.

Chairman MENENDEZ. OK.

Mr. EVANS. The regulators—the rationale that they gave us for stopping the Independent Foreclosure Review were concerns about potential outcomes, and they wanted to get money out quickly to potentially harmed borrowers. So we, in our report, we say that the achievement of the goals were hindered by a number of missteps by the regulators.

Chairman MENENDEZ. So let me ask you, and maybe Ms. Goldberg, one of the main purposes of the review was to have data to enable you to tell the bank had a particular kind of file or type of mistake that it was repeating so you could dig deeper into their other files. Since the OCC and the Federal Reserve abandoned the review, to what extent will they be able to further examine whether certain banks committed systematic errors in their foreclosures based on either preliminary results or based on information that they gathered through regular bank examinations or other sources?

Mr. EVANS. And I think that is the right question, and I think there——

Chairman MENENDEZ. I only ask the right questions.

[Laughter.]

Chairman MENENDEZ. I am just kidding.

Mr. EVANS. I will——

Chairman MENENDEZ. I think it is an important question, though.

Mr. EVANS. It is, and I think that is a good place for me to assert that any information based on the IFR at this point should be deemed incomplete, and the data does not allow us to render any conclusions about error rates at a particular servicer or make comparisons across servicers despite what has been reported in the press. There were different degrees of completion across the servicers, variations in the type of files that were reviewed, and also, even if it were complete, depending on the sampling methods used, it is possible that this information would still have limits. So it is impossible to draw any inferences about the data because they are not representative. So we are limited in terms of what we actually know.

Now, the regulators could have additional information, additional judgments that may help them make decisions about safety and soundness and corrective actions, but at this point, we have not done that type of work to determine what we know and whether it is statistically valid.

Chairman MENENDEZ. Is that information that would be accessible to you if we asked you and charged you to do that?

Mr. EVANS. As part of our ongoing review, we will start to look at those issues. We are more than willing to discuss with your staff the protocols governing our audit documentation, including any legal or privacy considerations, such as those concerning banking information, or any agency determinations that might be relevant. But we will continue to do this work for you and have conversations with your staff.

Chairman MENENDEZ. Thank you.

Ms. Goldberg, do you have any comments about this?

Ms. GOLDBERG. Yes. I would add one thing, which is that one concern we had all along with the methodology was the potential problem that the files themselves would not be enough to understand the problems that borrowers experienced.

So, for example, one of the most common problems that borrowers encountered was servicers losing their documents and having to resubmit them over and over and over again, or borrowers being told the wrong information. You have to stop making payments before we can consider you for a loan modification, you know, things along those lines.

And it is not clear that anybody examining just the files would be able to tease out that kind of information and understand those kinds of errors. And in order to do that, what is really necessary is for whoever is doing the review to be talking, at least in selective cases, to homeowners themselves or to the advisers who work with them, housing counselors or attorneys.

That is something that never happened as part of this process. It would be wonderful if it were to happen as part of a follow-up review, because I think you are completely right that getting to the bottom of this and understanding more clearly what problems actually took place, you know, how widespread they were, where, what borrowers were affected, is a really important lesson for us to be able to take away from this whole crisis in order to prevent it from happening again.

Chairman MENENDEZ. I have a whole host of questions, but one more before I turn to Senator Merkley.

The OCC and the Federal Reserve determined that $8.5 billion would be enough to cover the harm caused to borrowers, yet we know from the GAO study that there were numerous issues with sampling and instructions to the independent consultants. So how could the OCC and the Federal Reserve possibly determine that $8.5 billion, which would include $3.6 billion in direct payments to borrowers, is enough money to help these victims?

Mr. EVANS. That question was outside the scope of this particular study, but it is a question that we will be considering going forward.

Chairman MENENDEZ. Well, it is a question that we are going to look to work with you. I know that Congressman Waters also has joined us in this effort from the House side. I really want to know that, because if people went through harm, then at the end of the day, you have to have the resources to address the harm. And to come to a figure that is defective, from my perspective, because you do not have the sound science, so to speak, to make that determination, is, at best, a guess.

Ms. Goldberg, do you have any comment on that?

Ms. GOLDBERG. I would say it is probably a lowball guess.

Chairman MENENDEZ. OK. Senator Merkley.

Chairman MERKLEY. Thank you very much, Mr. Chairman, and thank you all for your testimony.

Mr. Smith, I wanted to start with a feature that was well publicized of the National Mortgage Settlement which said, in many cases, banks essentially wrote off the second loan that they had in the portfolio while not lowering the first loan, which was the bulk of the challenge for the homeowner. They did this for families that essentially had a foreclosure, in other words, did little to help the homeowner. How did this process of basically acting only for the loan you hold and not for the one that would affect the core of the family's success come about? Why was that acceptable?

Mr. SMITH. Well, Senator, the question you asked is important. The structure of the settlement itself was—I got it—I am administering it the way I found it. And so the settlement allows for different valuations, credits for different kinds of second loan forgiveness. The highest credits would be for performing loans or for loans where there is a—where it is done in conjunction with a first loan reduction so that you have more affordability. But the data does not show that a lot of that has been done to date.

The settlement does permit credit—at ten cents on the dollar, by the way, not dollar-for-dollar—for expungement of second liens as a goal in the effort—what the settlement documents say is to increase the prospects for future home ownership by the borrower.

It has been brought to my attention and it has been in the public domain, a discussion about the issue of whether, in certain circumstances, a second lien release does the borrower any good. I will say the fact that a loan has been written down, of course, does not mean it is—the loan itself is still a legal obligation of the borrower, even after foreclosure in and of itself, in some States, not all, it would be an obligation. So it is not clear that it will not always benefit the borrower.

But I think what the settlement does do is to credit second lien forgiveness most where they do the most good from the perspective of the question you just asked and least where it does the least good, and that is about all I can say to answer your question.

Chairman MERKLEY. Thank you.

Mr. Holland, I want to turn to the consultants who worked on the IFR. We had testimony in front of Sherrod Brown's subcommittee that the folks, the consultants who worked on it, had no idea how it was that individual homeowners got placed into different categories of possible financial harm. It is my understanding that that decision was actually made by servicers. How is it that the consultants who were doing the reviews had no idea of how individual homeowners got into different categories of financial harm?

Mr. HOLLAND. When you say consultants, are you talking about the independent consultants?

Chairman MERKLEY. That is my understanding, yes.

Mr. HOLLAND. I do not have knowledge of how that process, or how that process came about. We received the categorizations directly from the servicers and the OCC provided us with the dollar amounts that corresponded to those categorizations.

Chairman MERKLEY. How would the servicers who had not been the ones reviewing the files and had been essentially at the heart of so many pieces of this function possibly be a responsible party for putting people into categories of harm?

Mr. HOLLAND. I do not know. I do not have an answer for that question. I was not involved in that process.

Chairman MERKLEY. Ms. Goldberg.

Ms. GOLDBERG. I would like to correct one thing, Senator Merkley——

Chairman MERKLEY. Great. Thank you.

Ms. GOLDBERG. ——which is that when the independent reviews were stopped, the decision was made not to find harm, not to worry about finding harm. So the categories, as I understand it, the categories that borrowers were placed in for purposes of payments was based on how far along they had gotten in the loss mitigation process or the foreclosure process with their servicer.

So the fact that a particular borrower was in a particular category was not a reflection of whether they were actually harmed, but just kind of what stage of the process they had gotten to.

Chairman MERKLEY. I see.

Ms. GOLDBERG. But I think your fundamental question is a very good one. If we know that the servicers made the mistakes to begin with and we know that their systems were highly flawed, putting them in the position of slotting people into different categories seems unwise.

Chairman MERKLEY. Ms. Goldberg, when this IFR was announced, we had a hearing to have it explained to us and I raised the question on how is it that homeowners would feel confidence that their condition was going to be reviewed when they had had so many frustrating experiences to date and that the reviewers were being hired not by an independent strategy, but by the banks themselves, and that these reviewers were not third party, that they had clear financial connections to the banks themselves. I think then the fact that homeowners were promised a review and did not get the review just kind of, if you look at it from the street level, it seems like just one more farce. Is this far off the mark? That is a technical term, "farce."

[Laughter.]

Ms. GOLDBERG. Well, I would say that the feedback that we hear is a lot of frustration and disappointment and confusion from borrowers on the street who, I think, do not have confidence that this process played out in a fair and evenhanded manner.

Chairman MERKLEY. I have more questions, but I am over my time, so I will kick it back to the Chair.

Chairman MENENDEZ. Well, we will go through another round.

Let me ask, Ms. Goldberg, if the settlement provides around $5.5 billion in other forms of consumer mortgage-related relief, such as loan modifications and principal reduction—some people refer to that as soft dollars—so I would like to hear, to the extent that you know, more about how those soft dollars are being used to keep borrowers in their homes and how lenders are being credited under the IFR Settlement for taking such actions. For example, if a borrower has a $200,000 mortgage and receives $20,000 in mortgage relief, how is that relief calculated under the IFR Settlement? And are servicers doing all they can to keep homeowners in their homes?

And I would like to get a sense from Mr. Smith from the National Mortgage Settlement, how are those soft dollars calculated for that purpose under your settlement, and could you explain how each category is credited?

Ms. GOLDBERG. Thank you, Mr. Chairman. So, this process has not actually started yet, at least to the best of my belief, and I am not sure what the launch date will be, but we will get, hopefully, more information as time goes by.

But in terms of the way it is structured, what we know is that there are some specified categories of activity for which the servicers will get dollar-for-dollar credit. So that includes principal reduction, you know, loan modifications with principal reduction on first liens and second liens, short sales, and deeds-in-lieu of foreclosure. So for those four categories of activity, they will get dollar-for-dollar credit. So that is a difference from the National Mortgage Settlement, and Mr. Smith can explain those details much more accurately than I.

And in addition, another difference from the National Mortgage Settlement is that rather than getting credit for the amount—so let us take a loan modification—the amount by which the principal is reduced, the $20,000 in your example, servicers will get credit for the full unpaid principal balance of that loan, or the $200,000 in your example. So the borrower is still going to owe $180,000, and presumably with a loan modification will be able to repay that $180,000, and the $20,000 is really the benefit that they have experienced, but the servicer is going to get credit for the entire $200,000.

Chairman MENENDEZ. What is the public policy idea behind that?

Ms. GOLDBERG. I cannot answer that question. I cannot answer that question. I think that raises a lot of very serious concerns, some of which I mentioned in my testimony. And for us, one of the key ones is that——

Chairman MENENDEZ. If I can get ten times my investment of write-off, I would like to have that opportunity.

Ms. GOLDBERG. Right. And it certainly would encourage you, if you were the servicer, to do the biggest loans—you know, work on the biggest loans that you can because that is going to be the fastest route to meeting your goal, whatever that might be, for your soft dollar credits.

The downside of that is that the communities that we know experienced the most harm, low- and moderate-income communities and communities of color, where housing prices are lower and, therefore, loan balances are lower, it is going to take more of those loans to get to the same soft dollar goal, and the chances are too big in our estimation that those loans will be put aside. That is not where the priority will be focused, and instead it will be the higher-income, higher-balance loans that will get the first cut at the help.

Chairman MENENDEZ. That is a real concern. That is a real concern.

Mr. Smith, how does it work under your——

Mr. SMITH. Very well. Under the National Mortgage Settlement, there are certain categories of relief that are required to be not less than a certain percentage of total relief. And I would like to exclude, for a moment, only because it is somewhat separate, refinancing assistance is also required in each of the settlements, a specific dollar amount based on—there is a formula there, but it is essentially a multiplier based on yearly interest savings, or multiplied by a multiplier affecting the remaining maturity of the loan.

So that is—the principal forgiveness must comprise 60 percent of the total relief, soft dollar relief, credited otherwise, and I would like to emphasize credited because this is important. So, for example—and half of that 60 percent has to be first lien principal forgiveness.

Now, somewhat to Senator Merkley's point before. If a bank is a servicer and owner of a loan and forgives—and the loan has less than a 175 percent loan-to-value—I am going to simplify this slightly—but it is less than 175 percent LTV, owned and serviced—

let us say $45,000 is written down, $45,000 of credit is given. So the amount of relief and the credited amount are the same. If, on the other hand, a bank has originated a loan, is still servicing it, sells it into a securitization, to get $45,000 of credit, it has to write down $100,000. In other words, it is 45 cents on the dollar.

So that the thought, again, was—the theory, as I understand was, there was a concern about servicers getting credit for loans not owned by them. And so, at the very least, what the settlement does is to give less credit for that—in that circumstance. There is a different crediting for more than 175 percent.

Second liens, which have been discussed—forgiveness of a loan that is less than 90 days past due, or 90 days delinquent, which is different—delinquent—is 90 cents on the dollar. Ninety-one to 179 days is 50 cents on the dollar. And as I was saying before, 180 days or more past due is ten cents on the dollar.

So, again—but the amounts credited have to be—60 percent of the credited relief has to be principal forgiveness, and half of that, at least, has to be first lien principal.

In the case of ResCap, which we just did, actually, it was more than 50 percent was first lien forgiveness——

Chairman MENENDEZ. Well, that appears to be a far more equitable process than——

Mr. SMITH. And it goes on—and I could go on, but it is pages. But, I mean, for each category of relief, I do think—you can argue about the price, you can argue about the number of cents on the dollar, but I do think the settlement attempts to give credit that mirrors the benefit to the borrower, roughly, in a pretty good——

Chairman MENENDEZ. And that should, in my mind, be the principle.

Ms. GOLDBERG. And if I could add one thing, Senator, one other difference is—so Mr. Smith talked about the 60 percent of the credits under the National Mortgage Settlement have to be for principal reduction on first lien, right? That is what you said?

Mr. SMITH. Well, on the total. Thirty percent has to be——

Ms. GOLDBERG. OK. There is no kind of limits like that under the IFR settlement. So it would be possible for a servicer to meet their entire goal by doing short sales and deeds-in-lieu and be within the bounds of the settlement, as it is written.

Chairman MENENDEZ. And that would not necessarily maximize the goal of keeping people in their homes.

Ms. GOLDBERG. It would not.

Chairman MENENDEZ. Senator Merkley.

Chairman MERKLEY. Thank you very much, Mr. Chairman.

I wanted to continue on this same issue. In your testimony, Ms. Goldberg, on page ten, you note that on a loan with an unpaid balance of $500,000, a loan modification that provides any amount of principal reduction, be that $1,000 or $10,000 or $100,000, yields $500,000 worth of credit for the servicers. It is hard for anyone apart from this process to truly believe that if you do a $1,000 reduction, you get $500,000 credit. Yet are you saying, absolutely, that is the way it works?

Ms. GOLDBERG. That is what it says in the settlement. I have to say, Senator, that when I first read the settlement, I did not pick that up because it was so hard for me to believe it could be structured that way, as well. But, in fact, that is the wording of the settlement.

Chairman MERKLEY. Mr. Holland, is this accurate, to your knowledge?

Mr. HOLLAND. I have no knowledge of the way the settlement was written. In our role, you know, we have the administrative back-office tasks at hand—mailing, phone calls——

Chairman MERKLEY. But you have heard this issue. You have not found anything that contradicts what Ms. Goldberg has said?

Mr. HOLLAND. No. No, I have not.

Chairman MERKLEY. OK. Well, I would just like to point out that the roughly $6 billion in soft money that is in the settlement, at that 500-to-one rate, that is reduced down to $12 million. Six billion goes to $12 million. That is a vast difference.

Now, you have pointed out, Ms. Goldberg, that this creates a pure incentive to do reductions on large loans. Now, I live in a working class neighborhood, three-bedroom ranch houses. There are no $500,000 mortgages where I live because there are no $500,000 houses. So your point in your testimony is that working class communities, and certainly communities of color, are essentially—there is an incentive to kind of bypass them. Why would the Fed and the OCC agree to a structure that allows a 500-to-one or more—for that matter, it could have been one dollar under the argument you are making rather than a thousand—why would they agree to such a fictitious form of accounting and a structure that incentivizes the bypassing of working Americans in this whole process?

Ms. GOLDBERG. I think that is an excellent question, Senator Merkley. I am afraid I cannot answer it. It would be a good question to ask them to explain.

Chairman MERKLEY. Has anyone at the OCC or Fed explained, given a rational explanation of what they were possibly thinking?

Ms. GOLDBERG. At one point, I heard one person say that they believed that this structure accurately reflected the value of the assistance that the borrower received. That is the only explanation that I have heard, and it is not one that I find credible.

Chairman MERKLEY. Well, I am not sure how a borrower who gets $1,000 relief would feel they had gotten $500,000 of relief.

Ms. GOLDBERG. That is right.

Chairman MERKLEY. Well, and it is our working class neighborhoods that have been hit so hard, and in our communities of color where folks might have been more recent homeowners and had less equity, they were not in a case of losing a share of their equity. They were losing their entire house, and that brings us to the third point you have raised, which is that, essentially, there is no emphasis on saving the family, that a short sale gets the same value as preventing a foreclosure.

Ms. GOLDBERG. That is correct.

Chairman MERKLEY. Why would a settlement intended and publicized to help the homeowner put the same weight on a situation where a family loses a home as on a situation when a family is able to keep their home?

Ms. GOLDBERG. That is another excellent question to which I do not have an answer, and it is really because of those flaws, which we view as being extremely serious and severely undermining the potential benefit of this settlement, that—it is a done deal, right. The ink has dried on these settlements and I do not have this sense that there is any desire on the part of either the regulators or the servicers to go back and renegotiate them.

And so for us, that means it is really important to try and think about the places where something good can be rescued from this, and we see the two avenues to that being putting detailed information about who is getting help out there in the public arena, doing it regularly and in a timely fashion so that all of us can see who is and is not getting help and——

Chairman MERKLEY. So you are asking for——

Ms. GOLDBERG. ——and hope to help to shape that a little bit.

Chairman MERKLEY. You are asking for data on a census tract basis——

Ms. GOLDBERG. That is right.

Chairman MERKLEY. ——so this can truly be evaluated, which is transparency and accountability.

Ms. GOLDBERG. That is right.

Chairman MERKLEY. Is that guaranteed now, or does that require some future decision, and where would that decision-making power lie?

Ms. GOLDBERG. So, as I understand it, and I think as is actually reflected in the settlement itself, the servicers are required to report on a 45-day schedule to the regulators. I believe that they are still in the process of deciding which information that they will ask servicers to collect and report. And they have told us they are prepared to put some data out there in the public arena, but we do not know yet exactly what that will look like or how often that will be made available to the public, you know, when and how often.

Chairman MERKLEY. Mr. Chairman, I would be interested in pursuing this in partnership with you, that we should ask for such data to be part of this process for at least evaluation, looking back at what worked and what did not. Thank you.

Chairman MENENDEZ. Thank you. I am in agreement with the Senator. I will be happy to work with him.

Let me recognize our distinguished Ranking Member, Senator Moran, for any comments or questions.

STATEMENT OF SENATOR JERRY MORAN

Senator MORAN. Mr. Chairman, thank you.

I apologize for my lack of presence this morning. I am also the Ranking Member on an Appropriations Subcommittee that is meeting this morning with Secretary Duncan. But I wanted to at least make an appearance here at our first Subcommittee hearing and express my desire to be an active and full participant in this Subcommittee. I look forward to working with you, Mr. Chairman. Real estate, housing, is such an important component of the economy, but on a personal level, so important to individuals and their lives, their families.

And so I am only here for a few moments to make certain that you and others understand the desire on my part to work with you, to see that our Subcommittee fulfills its responsibility in oversight as well as in pursuing legislative proposals to meet the real estate and housing needs of our country. I look forward to working with you, Chairman Menendez.

Chairman MENENDEZ. Well, thank you very much, and we look forward to working with you, as well, and to our robust agenda that hopefully can continue to spur our housing market and solidify those who are in their homes, try to keep as many as possible and continue to make this a cornerstone of our American success for families. So thank you for coming by today.

I have another question or two, if I may.

The Foreclosure Review Payment Agreement provides almost two times the amount of relief to borrowers who requested a review compared to those who did not. In my previous hearing and throughout this process, I have expressed concerns about outreach efforts to our underbanked communities, and without documentations from these reviews, I believe it is safe to say we still do not know whether folks in these communities, who were greatly impacted, were ever aware of their right to review.

So my question is, are we giving the borrowers who may have never been contacted, therefore, who never requested a file review, the short end of the stick by offering them almost half of the relief as those who did request a review? Did you have any experience with that, Ms. Goldberg?

Ms. GOLDBERG. Yes. Thank you, Senator. So I think the GAO did an excellent job of outlining some of the problems in the outreach efforts around particularly the request for review part of the Independent Foreclosure Review, and we certainly had lots of concerns about communities in which people just were not aware that this process was going on. And I suspect if you stopped the average person on the street today, most of them would never have heard of the Independent Foreclosure Review.

I think as the result of the GAO's work, late in the game, the regulators made some very helpful changes in the way that they were doing outreach, in particular, working much more closely with community groups who could reach directly into the communities where response rates had been low and do a better job of making sure people knew that they had the opportunity to file a request for review.

And, indeed, in the last, I guess, 6 weeks or so of the year, right before the final deadline, the number of requests that came in went up significantly. But even at its high point, it was only, as I understand it, a little bit over 500,000 folks who filed a request for review out of four-point-some-odd million. So it is still 11 percent or something like that of the overall in-scope population who ever filed a request for review.

And my guess is that a great many people just never knew that was an option. They certainly, even if they knew it was an option, they did not know that it would have any impact on the amount of compensation that they would receive because that decision was not made until after the deadline passed to file a request for review.

So I have a grave concern about the level of differential in payment that is being awarded to people who filed a request for review and those who did not. As you point out, in many cases, it is double, and I think there are a lot of people who never knew this was an option for them who are suffering as a result.

Chairman MENENDEZ. As do I. If you knew that a review was likely to result in an increase in the relief that you received, then, number one, if you knew about the review process——

Ms. GOLDBERG. Right.

Chairman MENENDEZ. ——and, second, you knew that as a metric it would be more likely that you would receive greater relief, then it would be overwhelming that people would respond to receive the greater relief.

Ms. GOLDBERG. You would think so.

Chairman MENENDEZ. So this is a part of transparency that lacks here, because had that standard been set, we would have known. Mr. Evans, did you find this in your GAO report?

Mr. EVANS. Well, what I can say here is that, in terms of the recommendations we offered about the borrower outreach, the regulators did respond by targeting communities based on various characteristics, and they did increase their outreach efforts in terms of the print advertisements, the radio and television spots. And they also did some type of market analysis to identify areas and ethnic groups——

Chairman MENENDEZ. This is as a result of your——

Mr. EVANS. As a result of our recommendations. So that is someplace we can give the regulators credit, but——

Chairman MENENDEZ. All right. So let me—in the same vein, let me follow with Mr. Holland and Mr. Smith. I do not want you to feel out of the conversation, Mr. Holland, so I have a few. There is a reason you are here.

I understand it is a very large undertaking for your firm, and certainly the pressure on getting these payments out in a proficient manner, so I appreciate you coming before the Committee today. But as you may know, the IFR had many flaws related to outreach, to materials, to assistance for those who speak languages other than English as their man language. Can you provide an update on the efforts that your company is taking to make sure we do not make the same mistakes this time around as we did with the IFR?

For example, what channels are available to homeowners who contact Rust if they have questions or issues that need to be addressed? What steps or action plans are in place to actively or effectively communicate with borrowers? If somebody calls Rust and English is not their dominant language, are there other language abilities to be dealt with? Give me a sense of how you are working your job of this.

Mr. HOLLAND. Right. We have a call center and we are taking calls currently from people who have received the postcard notice as part of the settlement. And now, our first wave of checks that went out on Friday. So we do have the phone bank ready to answer any and all questions that we get from affected borrowers.

We have on-site Spanish-speaking operators that can assist Spanish-speaking people. And there is a process by where we can use a third party to help translate, I believe it is up to 200 languages, if somebody calls and has a language that we are not supporting live with Spanish or English. And we can get an operator on the phone that can help them.

In terms of your other question about are we making efforts to reach out to people, we have had the data, the mailing data for this group of people going back to the IFR, and it went through several levels of mailing address correction that we performed. So when we had the settlement, we started with that address information and, once again, ran it through the National Change of Address data base, and we are mailing checks to the best address that we have currently.

Some of those will be returned as undeliverable and we will make other attempts to find better address information for those that are undeliverable. And there is nothing in place yet, but we have had conversations about taking additional steps beyond what we have done in terms of address trace. We could implement an outbound calling program, email blasts. There are all sorts of things that may be available to us, nothing set yet, but those discussions are happening.

Chairman MENENDEZ. Those are discussions with the servicers?

Mr. HOLLAND. With the OCC and the FRB.

Chairman MENENDEZ. With the OCC and the FRB.

Mr. HOLLAND. And to the extent that, you know, even to the extent that somebody may receive a check and lose it, we will have information from the bank that shows us which checks are cleared, which checks are not. The regulators have said they want to leave the account open for up to 2 years, so that will give us ample time to even investigate those who do not cash checks, and then we can reach out to them to make sure that they received it and they get a chance to cash it.

Chairman MENENDEZ. Mr. Smith, with the National Mortgage Settlement, it required those five major mortgage servicers to comply with extensive servicing standards, including requiring a single point of contact for borrowers, adequate staffing levels and training, better communication with borrowers, appropriate standards for executing documents in foreclosure cases, ending improper fees, ending dual-track foreclosures for many loans.

Now, there have been some reports that there are abuses that are still occurring, even for borrowers that are part of the settlement. Can you provide an update on what you are seeing and hearing as it relates to these mortgage servicing standards. How far along have the lenders come in terms of implementing the new standards, and give us a sense of how that is moving forward.

Mr. SMITH. I will, Senator. Well, the standards were in place effective October 2nd or 3rd, 2012, so they are all to be applicable now. A thing that needs to be understood about the settlement is that my enforcement capacity, as I said in my written and oral testimony, is based on metrics which are tests of particular aspects of the standards.

We will issue our first report—we intend to issue a report on our initial testing of that performance in May. I mean, I say "intend" only because these are—we are doing a very thorough job, and if I have learned one thing from what I have heard today, it is do not rush to judgment. We are going to be sure we do a thorough job before we issue a report to the court and to the public. But I think I am hopeful that it will get done by the end of May. This will give us the beginning of insight based on sampling under the settlement, which, by the way, will be done under consistent standards that will be comparable across servicers. So we will be able to compare performance. And so I am hopeful that will begin to be some answers for you.

In our work this year, and because I have gone out and talked to a number of people who represent distressed borrowers, we believe we need additional metrics, that the metrics we have are good, but we need to fill in some spaces, and so I am hopeful within the next month, also, to get some additional metrics out, including an additional one on—we have one on single point of contact that will be tested, will be in our first report. We need more. The metric is OK, but it needs supplementation. And I think in a couple of other topics, we will do the same thing.

I think it is—I will tell you about a conversation one of my colleagues—to answer your question, generally, how they are doing, one of my colleagues, Josh Stein, had a Skype conversation with New Jersey advocates and counselors this last week. And what he heard were two things, and I want to make sure I will tell you both.

The first was that they are beginning to see an increase in responsiveness by the servicers over what they had experienced in the past. Quicker responses. They may not like the responses, but they are getting it quicker. Less lost documents. Less static. Not no static, but less. They did not say they were satisfied. There are still issues of concern and contention that need to be worked out. We have got a long way to go.

And so I think the fair thing to say is, I believe we are better off now than we were a year ago as a result—at least with regard to the five, as a result of the settlement. But I am not declaring victory. I think we have got a lot more work.

Chairman MENENDEZ. And just to follow up on your answer, all the elements that I mentioned that are part of the settlement, do you have metrics as it relates to all of those elements?

Mr. SMITH. No. I cannot honestly say that. I think the metrics—I think it is fair to say that the metrics cover a broad enough representation of what is required under the settlement to be pretty representative. But the short answer to your question is there are—I have got it here, actually—113 of the 304 are mapped to particular—of the standards are mapped to metrics. That leaves a number not mapped. So what we are doing, Senator, I think it is fair to say, is to give, I believe, a good insight and a good—we will give a good representation of where the servicers are. But it is supplemental to what their primary regulators, what the CFPB and others need to be doing going forward.

Chairman MENENDEZ. So let me close with one other question to you, which is in line with some of what we are talking about. I understand that most of the information that you are now able to report has been self-reported by the banks. Is that accurate?

Mr. SMITH. Yes.

Chairman MENENDEZ. OK. And while I am somewhat troubled by that idea, because that has not been a particularly good record by some of these institutions, can you explain what authority you have as the monitor to verify the information you receive from these servicers? How are you able to determine from the data that your most recent reports will be accurate? And is there any policy in place that would allow you to verify information in cases where you felt the self-reporting data lacked accuracy?

Mr. SMITH. Yes. The short answer—first, the self-reporting is the servicer, that is to say the firm, reports responses to these metrics, the questions on the metrics test. The servicers are required by the settlement to establish an Internal Review Group, which is to be separate from the mortgage servicing and the mortgage line of business. So it is—I would analogize it to the independent audit capacity in most organizations, which is to report separately outside the business operation.

That Independent Review Group will itself assess whether it agrees. It will test itself and will test whether it agrees with the servicer's assertion of compliance or if—of compliance. I then have an accounting firm of my own which reviews the work papers that the IRG has produced and has the capacity—and we have done additional tests and we have asked additional questions and we are going to—we are doing our best to tease out of all what we have gotten, all the information you can get to assure that what they are telling us is true. The one reason I cannot tell you for sure we are going to report in May is because we having prayer, shall I say, over a bunch of items now with regard to some of the servicers.

So we will—we are—what we have got is what I would say is a targeted approach to determining compliance. But we are going to do our very best to assure that we get everything we can out of that process and publicly report it so you can review and see what you think, how you think we did. I mean, I think—I am under no illusion that what we report will not be widely read and discussed, and that is good. That is intentional.

Chairman MENENDEZ. Well, I can assure you it will be widely read by this Committee, so——

Mr. SMITH. I am sure it will.

Chairman MENENDEZ. Let me thank you all for your testimony. It has been very elucidating in many respects. I have real concerns, as I have expressed early on to the regulators about this, and unfortunately, my concerns that were expressed going back some time ended up being, unfortunately, the reality.

It is the intention of this Committee to continue to pursue all the elements of this as we move forward with the regulators. I think that Ms. Goldberg's suggestions, making the best of what we have right now, are important ones and we look forward to pursuing that, as well. At the end of the day, those who were harmed should have the appropriate relief. They should know what that relief can be. They should be able to maximize that relief, and it seems to me a little perverse that you can get a lot—that the servicers, the institutions can get a lot but do a little in comparative ways, much different than the National Mortgage Settlement process. So those are real concerns to me as the Chair and I will look forward to continuing to pursue these. This record will remain open for 2 days for any Members who have questions for the record.

And with the thanks of the Committee, this hearing is adjourned.

[Whereupon, at 11:12 a.m., the hearing was adjourned.]

[Prepared statements and responses to written questions supplied for the record follow:]

PREPARED STATEMENT OF LAWRENCE L. EVANS, JR.

DIRECTOR, FINANCIAL MARKETS AND COMMUNITY INVESTMENT, GOVERNMENT ACCOUNTABILITY OFFICE

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Testimony

Before the Subcommittee on Housing, Transportation, and Community Development, Committee on Banking, Housing, and Urban Affairs, U.S. Senate

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FORECLOSURE REVIEW

Lessons Learned Could Enhance Continuing Reviews and Activities under Amended Consent Orders

Statement of Lawrance L. Evans, Jr., Director
Financial Markets and Community Investment

GAO
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Chairman Menendez, Ranking Member Moran, and Members of the Subcommittee:

I am pleased to be here today to discuss the Independent Foreclosure Review process. In April 2011, the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (Federal Reserve), and the Office of Thrift Supervision (OTS) issued consent orders against 14 mortgage servicers. These orders required the servicers to engage third-party consultants to review servicers' loan files to identify borrowers who had suffered financial harm due to errors, misrepresentations, or other deficiencies in foreclosure processing and recommend remediation for the harms these borrowers suffered.[1] Roughly 4.3 million borrowers who were in some stage of foreclosure in 2009 and 2010 were eligible for the foreclosure review.[2] As of December 2012, consultants had more than 800,000 loans slated for review. In January 2013, the regulators announced agreements that led to amended consent orders with 11 of the 14 servicers to discontinue foreclosure reviews and replace the reviews with a compensation framework that does not rely on determinations of whether borrowers suffered financial

[1]The 14 servicers that entered into consent orders with OCC, OTS, and/or Federal Reserve were Ally Financial, Inc.; Aurora Bank, FSB; Bank of America, N.A.; Citibank, N.A.; EverBank Financial Corp.; HSBC Bank USA, N.A.; JPMorgan Chase, N.A.; Metlife Bank, N.A.; OneWest Bank, FSB; PNC Bank, N.A.; Sovereign Bank; SunTrust Bank, Inc.; U.S. Bank, N.A.; and Wells Fargo Bank, N.A. and their affiliates or acquired loan servicing companies. The Federal Deposit Insurance Corporation (FDIC) was also a party to the Federal Reserve's order with Ally Financial (GMAC Mortgage). The Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §§ 311-313, 124 Stat. 1376, 1520-1523 (2010), eliminated OTS and transferred its regulatory responsibilities to OCC, FDIC, and the Federal Reserve. The transfer of these powers was completed on July 21, 2011, and OTS was officially dissolved 90 days later (Oct. 19, 2011).

[2]Borrowers were eligible to be included in the foreclosure review and have their loan files reviewed for errors if foreclosure actions took place on their primary residences between January 1, 2009 and December 31, 2010, by one of the participating servicers.

harm.[3] The remaining 3 servicers, covering 450,000 borrowers (10 percent), are continuing with the foreclosure review work.[4]

My remarks today are based on our March 2013 report on the implementation of the foreclosure review and lessons learned that can be applied to the activities required by the amended consent orders and ongoing foreclosure reviews.[5] My statement addresses (1) challenges to the achievement of the goals of the foreclosure review, (2) the extent of transparency in the foreclosure review process, and (3) lessons that could be useful for the activities under the amended consent orders and continuing reviews. As noted in our report, we were in the process of reviewing other aspects of the foreclosure review when OCC and the Federal Reserve announced the agreements. Neither our report nor this statement assesses the regulators' rationale for accepting the agreements nor any trade-offs involved in the regulators' choice to amend the consent orders with the servicers.

In summary, we found the following:

- Regulators' ability to achieve the goals of the foreclosure review was affected by the complexity of the reviews, as well as by overly broad

[3]OCC and the Federal Reserve announced on January 7, 2013, that they had reached agreements with 10 mortgage servicers. Those servicers are Aurora, Bank of America, Citibank, JPMorgan Chase, MetLife Bank, PNC, Sovereign, SunTrust, U.S. Bank, and Wells Fargo. On January 18, 2013, OCC and Federal Reserve announced that an agreement had been reached with HSBC. While not part of the original consent orders issued in April 2011, two additional institutions, Goldman Sachs (Litton Loan Servicing, LP) and Morgan Stanley (Saxon Mortgage Services, Inc.), also entered into consent orders with the Federal Reserve in 2012 that required a foreclosure review for deficient practices in mortgage loan servicing and foreclosure processing. The Federal Reserve announced on January 16, 2013, that it had reached agreements with these two servicers. Collectively, these 13 servicers are identified as the participating servicers in the agreements; however, Goldman Sachs and Morgan Stanley were outside the scope of our study because they were not part of the original 2011 consent orders.

[4]The servicers not participating in the agreements are Ally Financial (GMAC Mortgage), EverBank, and OneWest.

[5]GAO, *Foreclosure Review: Lessons Learned Could Enhance Continuing Reviews and Activities Under the Amended Consent Orders,* GAO-13-277 (Washington, D.C.: Mar. 26, 2013). This report represents the second phase of our examination of the foreclosure review process. In a previous report, we reviewed servicers' outreach efforts to inform borrowers of the foreclosure review; see GAO, *Foreclosure Review: Opportunities Exist to Further Enhance Borrower Outreach Efforts,* GAO-12-776 (Washington, D.C.: June 29, 2012).

regulator-issued guidance and limited monitoring for the consistency and sufficiency of consultants' review activities. For example, regulators' statistical sampling approach did not include mechanisms to allow the regulators to monitor consultants' progress toward finding as many harmed borrowers as possible. Our prior work has identified practices, such as assessing progress toward goals and designing monitoring during the planning stage of a project, as effective management practices.[6] In addition, the Office of Management and Budget (OMB) has found that in planning data analysis activities, such as sampling, agencies should take necessary steps to ensure that they have collected the appropriate data from which to draw conclusions.[7] Without using objective measures to compare review methods or assess sampling among consultants, regulators' ability to monitor progress toward achievement of foreclosure review goals was hindered.

- Although regulators publicly released more information on the foreclosure review process than is typically disclosed in connection with a consent order, the absence of timely and useful communication to the general public and individual borrowers at certain stages of the process impacted transparency and public confidence. To promote transparency, OCC and the Federal Reserve released redacted engagement letters between servicers and consultants, among other documents. However, some stakeholders felt there were gaps in the publicly released information, including the lack of detailed information on how the reviews were to be carried out. In addition, although borrowers who requested reviews under the foreclosure review process received an acknowledgement letter, some borrowers did not receive updates on their request for almost a year after the program was launched.

[6]See GAO, *Agency Performance Plans: Examples of Practices that Can Improve Usefulness to Decisionmakers*, GAO/GGD/AIMD-99-69 (Washington, D.C.: Feb. 26, 1999) and *Executive Guide: Effectively Implementing the Government Performance and Results Act*, GAO/GGD-96-118 (Washington, D.C.: June 1996). These reports identify and describe practices to improve the usefulness of agencies' annual performance plans and successfully implement results-oriented-management initiatives.

[7]OMB, *Standards and Guidelines for Statistical Surveys* (Washington, D.C.: September 2006). This document provides 20 standards that apply to work with the statistical purposes of describing, estimating, or analyzing the characteristics of groups, segments, activities, or geographic areas.

- The foreclosure review experience revealed lessons related to planning, monitoring, and communication that could help inform regulators' implementation of the amended consent orders and the remaining foreclosure reviews. In our prior work, we found that assessing lessons learned from previous experiences, such as through discussions with key participants and stakeholders, and applying these lessons can help strengthen future activities.[8] Without assessing and applying relevant lessons learned, regulators might not address similar challenges in activities under the amended consent orders or in the continuing reviews. In particular, regulators announced the agreements that led to the amended consent orders without a clear communication strategy, including determining what information to provide to borrowers. GAO's internal control standards and our work related to best practices indicate that an effective communication strategy and timely reporting can enhance transparency and public confidence.[9] Absent a clear strategy to guide regular communications with individual borrowers and the general public, regulators face risks to transparency and public confidence similar to those experienced in the foreclosure review.

Based on our findings, we recommended that OCC and the Federal Reserve improve oversight of sampling and consistency in the continuing reviews; apply lessons in planning and monitoring, as appropriate, to the activities of the amended consent orders and continuing reviews; and implement a communication strategy to keep stakeholders informed. The regulators agreed to take steps to implement these recommendations.

For our March 2013 report, on which this testimony is based, we analyzed consultants' sampling plans; reviewed relevant documents from

[8]GAO, *Federal Real Property Security: Interagency Security Committee Should Implement a Lessons-Learned Process,* GAO-12-901 (Washington, D.C.: Sept. 10, 2012) and *NASA: Better Mechanisms Needed for Sharing Lessons-Learned,* GAO-02-195 (Washington, D.C.: Jan. 30, 2002).

[9]See GAO, *Standards for Internal Controls,* GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999), *Troubled Asset Relief Program: One Year Later, Actions Are Needed to Address Remaining Transparency and Accountability Challenges,* GAO-10-16 (Washington, D.C.: Oct. 8, 2009); *Troubled Asset Relief Program: Additional Actions Needed to Better Ensure Integrity, Accountability, and Transparency,* GAO-09-161 (Washington, D.C.: Dec. 2, 2008); *Troubled Asset Relief Program: Status of Efforts to Address Transparency and Accountability Issues,* GAO-09-539T (Washington, D.C.: Mar. 31, 2009); and *Troubled Asset Relief Program: June 2009 Status of Efforts to Address Transparency and Accountability Issues,* GAO-09-658 (Washington, D.C.: June 17, 2009).

regulators, such as regulator-issued guidance to third-party consultants, law firms, and local examination teams, describing steps taken to foster consistency; reviewed regulators' communication materials; and interviewed five consultant teams, regulator staff, and consumer groups. We then compared this information and these parties' actions to criteria, such as the regulators' standard practices and policies, regulators' goals for the reviews, and our previous work. For those third-party consultants we did not interview, we obtained written information from them to address our objectives. We conducted the performance audit on which this statement is based from July 2012 through March 2013 in accordance with generally accepted government auditing standards.

Background

In September 2010, allegations surfaced that several servicers' documents accompanying judicial foreclosures may have been inappropriately signed or notarized.[10] In response to this and other servicing issues, federal banking regulators conducted a coordinated on-site review of 14 of the largest mortgage servicers to evaluate the adequacy of the controls over servicers' foreclosure processes and assess servicers' policies and procedures for compliance with applicable federal and state laws. On the basis of their findings, the regulators issued the April 2011 consent orders against these servicers that required the servicers to conduct the foreclosure review, among other things.[11] In January 2013, OCC and the Federal Reserve reached agreements with 11 of the 14 mortgage servicing companies subject to the April 2011 consent orders to discontinue the foreclosure reviews and to provide approximately $3.4 billion in direct payments to eligible borrowers. These agreements were formalized in amended consent orders that the regulators released in late February 2013. As shown in table 1, with this change from the foreclosure review to an agreed-upon payment process, regulators and servicers shifted from identifying the types and extent of

[10]This practice, which includes bank employees or contractors automatically signing foreclosure documents without verifying the details contained in the paperwork or the validity of the accompanying affidavits, became widely known as "robo-signing." Failure to review documents filed in connection with a judicial foreclosure may violate consumer protection and foreclosure laws, which vary by state and which establish certain procedures that mortgage servicers must follow when conducting foreclosures.

[11]The foreclosure review process had two components: a process for eligible borrowers to request a review of their particular circumstances (referred to as the borrower outreach process) and a review of categories of files (referred to as the look-back review).

harm borrowers may have experienced to instead focus on assigning all eligible borrowers into categories based on objective criteria. In addition, under the amended consent orders, the servicers also will provide approximately $5.4 billion in foreclosure prevention assistance to borrowers, such as loan modifications. Consultants for the servicers that did not reach agreements with the regulators continue their foreclosure review activities.

Table 1: Comparison of Borrower Payment Determinations between the Foreclosure Review and Amended Consent Orders

	Foreclosure review	Amended consent orders
Purpose of payment	Remediate borrowers who suffered financial harm as a result of servicer errors, misrepresentations, or other deficiencies[a]	Provide cash payments to all eligible borrowers
Borrowers assessed	Sample of eligible borrowers plus all borrowers in certain categories, including borrowers who submitted a request-for-review[b]	All eligible borrowers
Categorization process	Consultant reviews loan files for errors and categorizes borrowers	Servicer reviews information in their systems and categorizes borrowers[c]
Categorization criteria	Type of financial harm resulting from identified servicer error	Borrower and loan characteristics
Payment categories	Borrowers may be eligible for payment in multiple categories of harm	Borrowers eligible for payment in one category

Source: GAO analysis of OCC and Federal Reserve information.

[a] In addition to direct payments, borrowers who suffered financial harm may receive other types of remediation, such as correction of credit reports or, when possible, rescission of the foreclosure.

[b] Regulators expressly allowed third-party consultants to use sampling. Regulator staff told us that if third-party consultants' initial analyses of sampled loans identified errors, consultants were expected to use this analysis as the basis for a second sampling phase.

[c] In most cases, servicers, with regulators' approval, engaged the third-party consultants to review borrowers' files in two categories (Servicemembers Civil Relief Act and foreclosed borrowers who were not in default) to determine whether borrowers experienced those specific types of harm.

Complexities of the Foreclosure Review Process and Limitations in Regulators' Guidance and Monitoring May Have Hindered Achievement of Goals

Complexity of the file reviews, overly broad guidance, and limited monitoring for consistency may have impeded the ability of OCC and the Federal Reserve to achieve the goals of the foreclosure review. These goals were to ensure similar results for similarly situated borrowers, identify as many harmed borrowers as possible, and restore public confidence in the mortgage market. According to regulator staff and third-party consultants, coordinating the foreclosure review process was challenging because of the large number of actors and borrowers eligible for review, the size of the loan files, and the scope of the file reviews. In addition, each servicer had a unique process for recording and storing information on borrowers' loan files, which made defining review parameters and developing a uniform review structure that was appropriate for all consultants challenging.

Regulators took a number of oversight steps to address the complexities and challenges, including issuing nearly identical sections of the consent orders outlining the purpose of the foreclosure reviews, providing third-party consultants with guidance to help frame the file review process, and implementing regular communication mechanisms among the key actors to help foster consistency in the reviews. However, broad guidance and limited monitoring for consistency reduced the potential usefulness of information being collected and increased risks of inconsistency. According to third-party consultants, regulators' guidance did not address certain aspects of the foreclosure review, and consultants had to use additional judgment and interpretation when applying certain guidance, increasing the risk of inconsistency among review results. Third-party consultants and their respective law firms we interviewed said that they each developed their own test questions based on analyses of state foreclosure laws, loan modification guidelines, and bank policies, among other references.[12] According to OCC staff, the state law references were fairly straightforward and they had confidence that the consultants and law firms would provide fairly consistent interpretations. However, according to third-party consultants and law firms we interviewed, compiling these references and using them to develop review questions was challenging and time consuming and, in some cases, required judgment or interpretation of the laws or guidelines.

Regulators took steps to monitor potential inconsistencies among the reviews, but these steps were limited and likely would have resulted in delays in providing remediation to borrowers. Our prior work has identified using intermediate activities or measures to assess progress toward intended results as an effective management practice to understand the extent to which activities are on track to reach stated goals.[13] We have found that such activities can help management target areas that need improvement and select appropriate methodologies to realize that improvement. OCC and Federal Reserve staff said they had planned to assess the extent of inconsistencies affecting the outcomes for borrowers across the reviews after the reviews and recommendations for remediation were completed. However, conducting such an assessment after the completion of the reviews could have resulted in consultants

[12]To assess each of the review areas, consultants developed a series of test questions—generally yes or no questions—to identify potential errors.

[13]See GAO/GGD/AIMD-99-69 and GAO/GGD-96-118.

needing to re-do file reviews, which would have led to delays in remediation.

Other guidance issued by regulators did not specify key sampling parameters for the file reviews, and regulators lacked objective monitoring measures, resulting in difficulty assessing the extent of borrower harm. For example, our analysis of the May 2011 guidance on sampling found that the guidance was ambiguous about a key sampling parameter that resulted in variations in sample sizes used by the consultants and led consultants to use different triggers to determine when to conduct additional analysis. This ambiguity could have produced inconsistent results for similarly situated borrowers. According to OCC staff, they recognized that some consultants had not fully implemented the sampling approach as expected, and OCC is taking steps to address these differences for one of the servicers continuing the foreclosure review. In addition, our analysis found that the May 2011 guidance did not include a discussion of regulators' expectations for reporting on sampling, and variations among the sampling plans would have limited the types of information that regulators could report.

Finally, the regulators' sampling approach did not include key oversight mechanisms to facilitate assessment of whether consultants' reviews were sufficient to realize the goal of identifying as many harmed borrowers as possible, except in those cases where there were few or no errors. The OMB standards for statistical surveys state that where sampling is used, it should include protocols to monitor activities and provide information on the quality of the analyzed data.[14] Good planning and objective data collection provide a basis for making sound conclusions. In the absence of objective measures to compare review methods among consultants or assess sampling, regulators did not have an early warning mechanism to help identify problem areas that may have hindered achievement of the foreclosure review goals.

[14]OMB, *Standards and Guidelines for Statistical Surveys*, September 2006.

OCC and the Federal Reserve acknowledged the importance of transparency in the foreclosure review process and publicly released more information than is typically disclosed in connection with a consent order.[15] For example, regulators released redacted engagement letters between servicers and third-party consultants and the remediation framework for consultants to use that provided examples of situations in which compensation or other remediation is required for financial injury due to servicer errors, misrepresentations, or other deficiencies. However, the absence of useful and timely communications at certain stages of the process—for the general public as well as individual borrowers—hindered transparency and public confidence in the processes and results.

Some stakeholders perceived gaps in key information about how the file reviews were being conducted. Regulators did not release any additional guidance documents, nor did they publicly disclose consultants' test questions. To increase the transparency and credibility of the foreclosure review, consumer groups recommended that regulators release such information. According to consumer groups, without such information, the public would have questions and doubts about how the reviews were being executed. OCC and the Federal Reserve staff said that they considered releasing additional guidance to the public, but both expressed concerns that releasing detailed information risked disclosure of confidential or proprietary information. Moreover, test questions developed by consultants were numerous and complex, and Federal Reserve staff stated that review processes were too dissimilar to provide a comprehensive summary.

Borrowers who requested reviews under the foreclosure review process initially received limited information about the status of their individual file review. Borrowers received a letter acknowledging their request was

[15] By law, federal banking regulators must disclose any formal enforcement actions entered into under the Federal Deposit Insurance Act. See 12 U.S.C. §1818(u). On a case-by-case basis, banking regulators may consider the release of information beyond the mandatory disclosures. The Freedom of Information Act (FOIA), 5 U.S.C. § 552, generally provides that any person has a right of access to federal agency records, unless the records, or any portion thereof, are protected from disclosure by one of FOIA's nine exemptions. Records pertaining to the supervision of financial institutions are subject to one of FOIA's exemptions. 5 U.S.C. § 552(b)(8). Despite that exemption, regulators may exercise discretionary disclosure authority under 12 C.F.R. § 4.12(c) and 12 C.F.R. § 261.14(c) for OCC and the Federal Reserve, respectively, to release records concerning financial institution supervision.

received, but some did not receive updates until almost a year after the outreach program was first launched, when they received a letter informing them of the continuing nature of the review. In letters to OCC and the Federal Reserve, consumer groups indicated that these borrowers were frustrated by the lack of information on their particular file review. Regulators indicated that additional status letters and information would be sent to borrowers with outstanding requests-for-review. However, regulators were still uncertain about specific information they would require servicers to share with both borrowers who would receive remediation and those who would not. Regulators have acknowledged the importance of transparency, but after announcing the agreements that led to the amended consent orders, they had not yet determined what information to convey beyond that which was included in their press releases and public websites and whether additional information would be provided to borrowers who submitted a request-for-review.

During the foreclosure review process, OCC released two interim reports that provided the public with information on the organization and conduct of the file review process and preliminary results, such as the number of requests-for-review received, for institutions it supervises. These reports, according to OCC, were intended to build transparency into the process. The Federal Reserve did not issue interim reports on the foreclosure review process for institutions it supervised. According to Federal Reserve staff, they did not do so because their public release of servicers' action plans provided sufficient information about how servicers were addressing the requirements of the consent orders and their public release of servicers' engagement letters provided sufficient information about how the foreclosure review would be conducted. Prior to the announcement of the agreements that led to the amended consent orders and ended the foreclosure review for most servicers, OCC staff told us they had planned to release a final report on the results of the foreclosure review, and Federal Reserve staff indicated they expect to publish additional relevant information related to the foreclosure review and the agreements. However, as of February 2013, regulators had not decided what information on the work conducted under the foreclosure review prior to the agreements will be made available.

The foreclosure review revealed three key lessons related to planning, monitoring, and communication that could help inform regulators' implementation of the amended consent orders and the continuing foreclosure reviews. These key lessons could help contribute to an effective process for distributing direct payments and other assistance as prescribed by the amended consent orders. Based on the foreclosure review experience, we found that (1) designing project features during the process's initial stages influences the efficiency of file reviews, (2) monitoring progress helps ensure achievement of goals, and (3) promoting transparency enhances public confidence.

Our prior work shows that assessing and using lessons learned from previous experiences can provide a powerful method of ensuring that beneficial information is factored into the planning and work processes of future activities.[17] Key practices of assessing lessons learned include collecting and analyzing information on prior activities and applying that information to future activities. Assessing lessons learned by using project critiques and discussions with key participants and stakeholders—such as local examination team staff, third-party consultants and law firms, and external groups—could identify the root causes of strengths and weaknesses of the foreclosure review that could apply to the amended consent order activities.

The foreclosure review experience suggests that a planning process to determine key project features, such as guidance and necessary data elements, for activities conducted under the amended consent orders could lessen the risk of changes to planned activities, future delays, or rework. Our work on designing evaluations, including financial audits, has found that systematic and comprehensive planning enhances the quality, credibility, and usefulness of the results and contributes to a more effective use of time and resources.[18] As regulators prepare to implement

[17]See GAO-12-901 and GAO-02-195. In GAO-02-195, we established a lessons-learned process based, in part, on research done by the Naval Research Laboratory at the Navy Center for Applied Research in Artificial Intelligence. In GAO-12-901, we updated this work through a literature review and interviews with agencies.

[18]In assessing the foreclosure review process, we considered our prior work on program evaluations, government auditing standards, and financial auditing. See GAO, *Designing Evaluations: 2012 Revisions,* GAO-12-208G (Washington, D.C.: January 2012); *Government Auditing Standards: 2011 Revision,* GAO-12-331G (Washington, D.C.: December 2011); and GAO and President's Council on Integrity and Efficiency, *Financial Audit Manual: Volume 1*, GAO-08-585G (Washington, D.C.: July 2008).

the amended consent orders, they risk having to make changes in the planned activities or publicly announced timelines if they miss opportunities to make key project planning decisions, including issuing clear guidance.

The foreclosure review experience also suggests that using mechanisms to monitor the amended consent order activities and the continuing foreclosure reviews may help ensure achievement of goals. The regulators' process for monitoring the activities of third-party consultants, servicers, and examination teams during the foreclosure review process could provide a useful model for monitoring activities under the amended consent orders. In addition, regulators' experience with the foreclosure review suggests that identifying comparative oversight mechanisms to centrally promote consistency and monitor activities under the amended consent orders could help achieve consistent results for borrowers. GAO's internal control standards state that agencies should take steps to comprehensively identify and analyze program operations to determine if risks exist to achieving goals—such as risks to the regulators' goal of providing similar results for similarly situated borrowers.[19] In our prior work, we found that using a horizontal review mechanism is an option to help mitigate risks of inconsistent results for activities conducted by multiple entities, such as multiple servicers.[20] Using mechanisms to centrally monitor the consistency of servicers' activities under the amended consent orders may lessen the risk of inconsistent results or delays in providing direct payments to borrowers. Similarly, monitoring potential inconsistencies for the servicers that are continuing the foreclosure reviews will provide regulators with information to assess whether there is a risk of those borrowers being treated inconsistently.

Finally, lessons from the foreclosure review activities conducted to date suggest that developing and implementing an effective communication strategy that includes public reporting goals could enhance the

[19]See GAO/AIMD-00-21.3.1.

[20]GAO, *Opportunities Exist to Apply Lessons Learned from the Capital Purchase Program to Similarly Designed Programs and to Improve the Repayment Process,* GAO-11-47 (Washington, D.C.: Oct. 4, 2010). In our analysis of the U.S. Department of the Treasury's oversight of the Capital Purchase Program under the Troubled Asset Relief Program, we found that Treasury's practice of establishing centralized control mechanisms to help ensure consistency of activities conducted by multiple banking regulators helped lessen the likelihood of inconsistent results.

transparency of the activities under the amended consent orders. GAO's internal control standards emphasize the importance of relevant, reliable, and timely communications both within an organization and with external stakeholders.[21] In addition, our work on the Troubled Asset Relief Program (TARP) has underscored the importance of a communication strategy to strengthen communication with external stakeholders and improve transparency and accountability.[22] Experiences with current government initiatives that are aimed at assisting struggling homeowners and involve institutions and mortgage-related issues similar to those of the foreclosure review highlight the benefits of regular performance reporting. Specifically, periodic reports on the performance of and participation in TARP programs and scheduled reports on servicers' compliance with requirements of the National Mortgage Settlement are intended to promote transparency and build public confidence.[23] Like TARP and the National Mortgage Settlement, the foreclosure review and the subsequent activities under the amended consent orders are part of the larger governmental response to the housing and mortgage crises. As a result, a communication strategy which incorporates plans for periodic public reporting may enhance transparency in the distribution of direct payments and other assistance and help restore confidence in mortgage markets.

Regulators announced the agreements that led to the amended consent orders without a clear communication strategy. As a result, what information will be provided to individual borrowers and the general public

[21]See GAO/AIMD-00-21.3.1.

[22]We have made a series of recommendations aimed at improving the transparency of TARP by ensuring that Treasury develops a comprehensive communication strategy. TARP, like the foreclosure review and subsequent activities under the amended consent orders, is one of many activities the federal government has put in place to respond to the financial crisis, including the crises in the housing and mortgage markets. As such, we believe that similar efforts to improve communication will enhance the transparency in the implementation of the amended consent orders and continuing foreclosure reviews. See GAO-10-16, GAO-09-161, GAO-09-539T, and GAO-09-658.

[23]The National Mortgage Settlement is the result of an agreement reached in February 2012 by the country's five largest mortgage servicers with the Departments of Justice, Treasury, and Housing and Urban Development and 49 state attorneys general. Under the terms of the settlement, Ally Financial (GMAC Mortgage), Bank of America, Citibank, JPMorgan Chase, and Wells Fargo will provide approximately $25 billion in relief to distressed borrowers in states that signed on to the settlement as well as direct payments to participating states and the federal government. United States v. Bank of America Corp., No. 1:12-CV-00361 (D.D.C. Apr. 4, 2012).

about processes, progress, and results of activities under the amended consent orders is unclear. OCC and the Federal Reserve have provided some information on the amended consent orders, and planned to release additional information, such as details on payment categories that were publicly released in April 2013. However, we found that as of March 2013, regulators had not made key decisions on communicating directly with individual borrowers and the extent to which they would report on activities related to the amended consent orders and continuing foreclosure reviews. While the amended consent orders terminate the foreclosure review for most of the servicers, transparency of past and current efforts continues to be important to stakeholders, including Congress and consumer groups. In the absence of a clear communication strategy to direct external communications, including public reporting and direct communication with individual borrowers, regulators face risks to transparency and public confidence similar to those experienced in the foreclosure review process.

In our March 2013 report, we recommended that OCC and the Federal Reserve improve oversight of sampling and identify and apply lessons from the foreclosure review process, such as enhancing planning and monitoring activities, to better ensure that the goals of the foreclosure review and amended consent orders are realized. In addition, to better ensure transparency, we recommended that OCC and the Federal Reserve develop and implement a communication strategy to regularly inform borrowers and the public. In commenting on the report, OCC and the Federal Reserve both identified actions that they have taken or planned to take to implement the recommendations.

Chairman Menendez, Ranking Member Moran, and Members of the Subcommittee, this concludes my prepared statement. I would be happy to answer any questions that you may have at this time.

If you or your staff have any questions about this testimony, please contact Lawrance L. Evans, Jr. at (202) 512-8678 or evansl@gao.gov. Contact points for our Offices of Public Affairs and Congressional Relations may be found on the last page of this statement. Other staff who made key contributions to this testimony include: John Karikari; Jill Naamane; Anna Maria Ortiz; Karen Tremba (Assistant Directors); Bethany M. Benitez; Charlene J. Lindsay; Patricia MacWilliams; Marc Molino; Robert Rieke; Jennifer Schwartz; Andrew Stavisky; Sonya Vartivarian; James Vitarello; and Monique Williams.

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PREPARED STATEMENT OF JOSEPH A. SMITH, JR.

MONITOR OF THE NATIONAL MORTGAGE SETTLEMENT

APRIL 17, 2013

Introduction

Thank you Chairman Menendez, Ranking Member Moran, and Members of the Subcommittee for inviting me today to testify about implementation of the National Mortgage Settlement. It is a pleasure to be here with you to talk about this important issue.

As you know, on April 5, 2012, the National Mortgage Settlement went into effect when the United States District Court for the District of Columbia entered five separate consent judgments that settled claims of alleged improper mortgage servicing practices against five major mortgage servicing organizations: Bank of America, N.A., CitiMortgage, Inc., JPMorgan Chase Bank, N.A., Residential Capital LLC and affiliates (formerly GMAC) and Wells Fargo & Company and Wells Fargo Bank, N.A. Government parties to the settlement include the U.S. Department of Housing and Urban Development, the U.S. Department of Justice, Attorneys General from 49 States and the District of Columbia, various State financial services regulatory agencies and other releasing parties, including the Consumer Financial Protection Bureau and the U.S. Department of Treasury.

The settlement was an unprecedented and collaborative bipartisan effort by the States and the Federal Government to improve the way mortgage servicers work with distressed borrowers while also providing much needed relief to homeowners across the Nation.

The settlement can be divided into three parts: direct payments to borrowers and States, consumer relief and servicing standards. While I have no oversight over the direct payments, as the monitor of the settlement, I am responsible for reviewing and certifying the discharge of the servicers' consumer relief obligations and overseeing their implementation of and compliance with the servicing standards.

Organizational Overview

As monitor, I am subject to oversight by a Monitoring Committee that is comprised of representatives of the U.S. Department of Housing and Urban Development, the U.S. Department of Justice, and representatives of 15 States. My office operates under a budget I prepare annually in consultation with the Monitoring Committee and servicers and is paid for by the servicers out of their corporate funds. My budget for fiscal year beginning July 1, 2012, was so prepared and is in effect. At the end of this fiscal year, I will make publicly available a report with audited financial statements covering my operations.

To assist me in enforcing the settlement, I am authorized to employ a primary professional firm (PPF) agreed to by the servicers. In selecting the PPF, my goal was to find a firm that not only had the organizational capacity and subject matter expertise to do the work well, but also was independent of all five servicers. I conducted a thorough selection process during which I invited 46 firms to submit a proposal and reviewed 23 proposals. At the end of this process, I retained BDO Consulting. BDO has substantial financial services industry experience, yet has no meaningful conflict with any of the servicers.

As the PPF, BDO is responsible for ensuring quality control and making sure that the review of the servicers' implementation of and compliance with the servicing standards is done in a consistent way. BDO is also responsible for reviewing and confirming the consumer relief that the servicers extend to borrowers under the terms of the settlement and has been performing that work to exacting standards over the last 6 months.

To assist in the review of servicer implementation of and compliance with the servicing standards, I also have retained five separate secondary professional firms (SPFs), including Baker Tilly Virchow Krause, LLP; BKD, LLP; Crowe Horwath LLP; Grant Thornton LLP; and McGladrey LLP. Each SPF is assigned to a specific servicer. As with BDO, each SPF is free of any relationship to its assigned servicer that would undermine public confidence in its work.

Each servicer also has an internal review group (IRG), or group of employees and/or independent contractors and consultants that is responsible for performing reviews of the servicer's compliance with the settlement and whose members are required to be separate and independent from the line of business being reviewed. My office and its associated professional firms have also reviewed the qualifications and resources of each IRG to ensure it has the capacity and independence to do a credible job.

In addition to the PPF and SPFs, the settlement authorizes me to retain attorneys and other professionals to help me carry out my duties. Accordingly, I have engaged the law firms of Poyner Spruill and Smith Moore Leatherwood; the forensic accounting firm of Parkside Associates; the accounting firm Cherry, Bekaert & Holland; and the communications firm Capstrat. As required by the settlement, each firm is independent of the servicers.

Though it was not required by the settlement, I have sponsored the creation of the Office of Mortgage Settlement Oversight (OMSO), a not-for-profit organization that provides administrative support for my work, including acceptance and payment of money and the maintenance of books and records. OMSO enables me to carry out my duties transparently and independently with administrative oversight from an independent Board of Directors.

Consumer Relief

Under the settlement, the servicers have agreed to provide specific dollar amounts of relief to distressed borrowers within a 3-year period. This relief includes first and second lien modifications, short sale assistance, deficiency waivers, forbearance for unemployed borrowers, antiblight activities, benefits for members of the armed services, and refinancing programs.

Within limits, the servicers have flexibility to apply these different kinds of relief as they see fit to meet their overall obligations. The settlement specifies that certain types of relief must make up a certain percentage of each servicer's commitment. For example, 60 percent of the total credited relief must come from first and second lien modifications; of that at least half must be modifications made on first liens.

Under the consumer relief terms of the settlement, the servicers are required to make quarterly reports to the States (with copies to the Monitoring Committee and to me) of relief during that quarter in each State and in the Nation as a whole. They have done so, in November of last year and February of this, and the data they provided was the basis of my progress reports to the public issued in the same months.

The kinds of consumer relief for which a servicer can receive credit under the settlement are set out in detail in the consent judgments and the credit varies based on the relief given. For example, servicers can receive dollar for dollar credit for principal forgiveness on loans both owned and serviced by the servicer and as little as five cents on the dollar for certain forbearance activities. For that reason, the gross dollar amounts of relief the servicers have delivered to homeowners far exceeds their total credited obligations under the settlement.

For each amount of relief it has provided to borrowers on or after March 1, 2012, a servicer will receive credit against the commitments it made when it entered the settlement. To encourage the servicers to make substantial progress in the first year of the settlement, it gives them an additional 25 percent credit for any credited first or second lien principal reductions or refinancing activities that take place within the 12 months after March 1, 2012. If a servicer's total commitment is not fully satisfied within 3 years, it will be required to pay a penalty of no less than 125 percent of its unmet commitment amount.

A servicer can choose to seek a determination by me of its satisfaction of its consumer relief obligations whenever it has asserted such satisfaction to its IRG, its IRG has confirmed such satisfaction and such confirmation is reported to me. In November 2012, the ResCap parties requested a satisfaction review. In February of this year, after a review of their performance, I issued a report confirming their satisfaction of their minimum consumer relief obligations and partial satisfaction of their mandatory solicitation requirements. My report was filed with the United States District Court for the District of Columbia and is available for review on my Web site. In February, each of the other four servicers requested a determination of partial satisfaction of their consumer relief obligations through December 31, 2012. A review of the assertions of completed consumer relief by the servicers and the confirmation of completion by their IRGs is in progress. I will publicly report my determination later this year after my review is done.

In their latest reports to the States, compiled in my most recent progress report, the servicers have reported that from March 1, 2012, to December 31, 2012, 554,389 borrowers benefited from some type of consumer relief totaling $45.83 billion, which, on average, represents about $82,668 per borrower. This figure includes both completed relief and active first lien trial modifications. The amounts reported are gross dollar figures rather than credited relief under the settlement and, except for amounts reported by the ResCap parties, have not been reviewed or scored by the PPF or by me.

Additional information with regard to consumer relief to date under the settlement is available in my most recent report, titled "Ongoing Implementation".

Servicing Standards

In addition to consumer relief, the settlement establishes 304 servicing standards, or rules of conduct, to which the servicers must adhere. These servicing standards are intended to redress the practices in mortgage servicing that led to the claims that resulted in the settlement. It is important to note that the servicing standards apply to all loans serviced by the servicers, regardless of the loan's owner. Each servicer has been responsible for implementation of and compliance with the standards since October 2, 2012.

There are servicing standards related to document integrity, the loan modification process, dual tracking, single points of contact, other customer service requirements, and other more general requirements.

Under the settlement, I am directed to measure servicer compliance with the servicing standards through 29 metrics—tests designed to determine whether one or more of the servicing standards are being followed. The servicers conduct these tests through their IRGs, who then report the results to me. Assisted by my PPF and SPFs, I assess the work of the servicers and report my conclusions. If the IRGs or I find potential violations—noncompliance with the standards—the servicer has to implement a corrective action plan and remediate any identified potential violations. In the case of a widespread error, the servicer has to search for all potential violations since implementation of the servicing standard and remediate them. If it can't or won't correct the potential violations, injunctions or civil penalties can be sought through the United States District Court for the District of Columbia.

We have completed our first review of servicer compliance under the settlement—for the calendar quarter ended on September 30, 2012—and have nearly completed our second quarterly review. When that review is complete, I will report to the Court and to the public on how the servicers have performed. I intend to deliver that report next month. This process will continue for the next 2 years.

Complaints

To help me better understand the settlement's impact in the marketplace, my colleagues and I closely review consumer complaints we receive through my office as well as the complaints elected officials escalate to the servicers. As part of the settlement's terms, the servicers are required to provide me with access to all the complaints submitted to them by Members of Congress, Attorneys General and other governmental agencies. I also have met with Attorneys General, their staffs, lawyers who represent borrowers and housing counselors in hard hit States such as Florida, Nevada, California, Illinois, and Arizona, and I look forward to doing as much more of this as is possible. Further, I have recently entered an information sharing relationship with the Consumer Financial Protection Bureau that has great promise.

Through the complaints and my meetings with Attorneys General staff, housing counselors and lawyers, I have learned about the issues that borrowers continue to experience. While I have heard about progress and success in obtaining consumer relief, problems with the servicing standards, including single points of contact, dual tracking and the loan modification process in general are still occurring all too often. These are the issues that guide my conversations with the servicers.

The settlement anticipated situations in which there would be issues surrounding servicing standards not tested by a metric and allowed me the opportunity to develop three discretionary metrics. As a result of what I have heard from consumers and professionals, I am now working with the servicers to establish my discretionary metrics. They are not yet completed, but they will address what I have learned in the last year.

Conclusion

In closing, the settlement has been successful in what I believe is a worthwhile effort: focusing resources on a specific problem in a targeted, time-limited way that augments and supports the work of policy makers and governmental agencies. I applaud the bipartisan leaders who crafted this settlement to address serious issues with local and national implications. Properly implemented and enforced, the settlement has the potential to result in a substantial public benefit. I look forward to continuing my work toward that goal and welcome your questions.

PREPARED STATEMENT OF DAVID HOLLAND

EXECUTIVE VICE PRESIDENT, RUST CONSULTING

APRIL 17, 2013

Introduction

My name is David C. Holland. I am an executive vice president based in Rust Consulting's Minneapolis, Minnesota, office. Rust Consulting, or "Rust," has been engaged by the servicers to administer certain aspects of the Alternative Resolution Settlement as directed by the Office of the Comptroller of the Currency (OCC) and the Federal Reserve Board (FRB). Previously, Rust was engaged by the servicers to administer the Consent Orders for the Independent Mortgage Foreclosure Borrower Outreach project, also known as the Independent Foreclosure Review (IFR).

Rust provides project management, data management, notification, contact centers, claims processing, and fund distribution, typically in support of large, complex, and time-sensitive programs. Rust has handled more than 4,000 programs in all.

Independent Foreclosure Review

Rust was originally engaged by 14 servicers to serve as the administrative provider under the IFR Consent Orders. Broadly speaking, our responsibilities under the Consent Orders were to notify homeowners about the program, to answer their questions, to receive their Request for Review forms, and to handle in- and outbound mail. From November 2011 through December 2012, we executed three mass mailings to homeowners. Over the same period and through January 2013, we received and forwarded homeowner Requests for Review forms.

Alternative Resolution Settlement

Rust was recently engaged by 11 of the 14 original servicers, along with two additional servicers, to serve as the Paying Agent under the Alternative Resolution Settlement (Settlement). Our responsibilities under the Settlement are to notify homeowners about this program, to answer their questions, and distribute settlement payments in the form of checks to eligible homeowners.

1. Rust updated the ending-IFR-program database of homeowner addresses through the National Change of Address service and mailed postcards on March 18, 2013, informing homeowners that they were eligible to receive a payment as a result of the Settlement.
2. Rust received relevant data from servicers that identified loan classifications for each individual loan and subsequently received data from the OCC and FRB detailing the payment amounts for each loan classification. The first wave of checks, approximately 1.4 million, were mailed on Friday, April 12. The majority of the remaining checks will be mailed in three more waves occurring on April 19, April 26, and May 3.
3. Rust continues to staff a call center to take incoming calls from homeowners with questions about the program and update the Web site for the IFR project to provide new information regarding the Settlement.

Outreach Efforts

At the direction of the servicers, the OCC, and the FRB, Rust implemented a number of address correction processes to maximize the number of homeowners who received notice as part of the IFR. Rust will continue to use address correction processes under the Settlement.

1. In both projects, the NCOA process was used to update addresses.
2. As part of the IFR, Rust received undeliverable notices, ran the corresponding addresses through a "skip-trace" process, and whenever possible, remailed notices to new addresses.
3. For any of the remailed notices that were returned as undeliverable, Rust performed another second type of address search, and again, whenever possible, remailed notices to new addresses.
4. Under the Settlement, Rust will receive undeliverable checks and attempt to find better addresses and, whenever possible, remail the checks to new addresses.

Reporting

During the IFR process, Rust provided comprehensive daily statistical reporting to the OCC, the FRB, independent consultants, and the servicers. Daily meetings were held with the consortium of the 14 servicers and independent consultants that covered the current state of project execution, future deliverables, and next-phase planning.

As part of the Settlement, Rust provides comprehensive daily statistical reporting to the OCC, the FRB and the servicers. Daily conference calls are held with the servicers covering project execution. Two times weekly, conference calls are held with the OCC and the FRB covering project execution and future deliverables.

PREPARED STATEMENT OF DEBORAH GOLDBERG

SPECIAL PROJECT DIRECTOR, NATIONAL FAIR HOUSING ALLIANCE

APRIL 17, 2013

Chairman Menendez, Ranking Member Moran, and Members of the Subcommittee, my name is Debby Goldberg, and I am a special project director with the National Fair Housing Alliance (NFHA). Founded in 1988 and headquartered in Washington, DC, the National Fair Housing Alliance is a consortium of more than 220 private, nonprofit fair housing organizations, State and local civil rights agencies, and individuals from throughout the United States. Through comprehensive education, advocacy and enforcement programs, NFHA protects and promotes residential integration and equal access to apartments, houses, mortgage loans, and insurance policies for all residents of the Nation.

I want to thank you for the opportunity to testify here today about the Independent Foreclosure Review (IFR). The IFR was one component of consent orders that the Office of the Comptroller of the Currency and the Federal Reserve Board signed 2 years ago with 14 mortgage servicers, later expanded to 16 companies. Those consent orders were intended to address widespread failures in those companies' mortgage servicing and loss mitigation systems, as identified in the "horizontal review" that the regulators conducted in the wake of the so-called robo-signing scandal.

NFHA and many other civil rights and consumer organizations welcomed the announcement that the regulators had entered into consent orders with these servicers and supported the dual goal of the orders: to ensure that the servicers made changes to their staffing, systems and oversight that would prevent future borrowers from experiencing the kinds of problems that could lead to unnecessary foreclosures; and to identify borrowers whose servicers acted improperly in the foreclosure process and the events leading up to it, and compensate those borrowers for the financial harm they suffered. We only wish that the announcement had come much sooner, so that some of the four million or more homes that have been lost to foreclosure since 2008 might have been saved.[1]

The Negative Impact of the Foreclosure Crisis on Communities of Color

For NFHA, the 2011 consent orders represented an important regulatory milestone. Four years earlier, in 2007, we and four other national civil rights organizations called for a national moratorium on foreclosures. We did so because we were hearing from our members and others about the massive level of foreclosure activity occurring in communities of color all across the country. The situation had reached crisis proportions and called for a national response. In previous years, communities of color had been flooded with subprime and other unsustainable mortgages. African American borrowers were 3 times more likely, and Latino borrowers were 2.5 times more likely to be placed in subprime loans than their white counterparts.[2] Research indicated that significant numbers of these borrowers had credit that was good enough to qualify them for safer, less costly prime loans.[3] Recent settlements between the U.S. Department of Justice and several major mortgage lenders illustrate how financial incentives encouraged mortgage brokers and loan officers to charge higher fees to hundreds of thousand of African American and Latino borrowers. These incentives also encouraged lenders to steer tens of thousands of borrowers who qualified for prime loans into subprime mortgages that were more profitable for the loan originators, but proved to be disastrous for the borrowers, their communities and our economy as a whole.

[1] CoreLogic, "CoreLogic Reports 767,000 Completed Foreclosures in 2012", February 1, 2013, available at *http://www.corelogic.com/research/national-foreclosure-report-december-2012. pdf.*

[2] Bocian, Debbie Gruenstein, Wei Li, Carolina Reid, and Roberto G. Quercia, "Lost Ground, 2011: Disparities in Mortgage Lending and Foreclosures", Center for Responsible Lending, November 2011.

[3] Brooks, Rick, and Ruth Simon, "Subprime Debacle Traps Even Very Creditworthy", *Wall Street Journal,* December 3, 2007.

While the foreclosure crisis has affected a great many borrowers and communities, some have been hit harder than others. According to research by the Center for Responsible Lending (CRL), by early 2011, 25 percent of all African American and Latino homeowners who had mortgages originated between 2004 and 2008 had either lost their homes to foreclosure or were seriously delinquent, a rate twice that of white borrowers. The impact of these foreclosures has been devastating, not only for the families who have lost their homes, but also for their neighbors whose lives and communities and property values have all be affected. CRL' s research indicates that $2 trillion of wealth has been lost as a result of the foreclosure crisis. Half of that amount, $1 trillion, has been lost by communities of color.[4] It may be a full generation or more before this lost wealth is regained, and the implications of this loss for our country are profound.

NFHA's own work shows that the negative impact of foreclosures lasts far beyond the event itself. We have investigated the practices of mortgage servicers with respect to maintenance, management and marketing of the homes they have taken back through foreclosure (i.e., their real-estate owned or REO properties). We have found that, compared to REO homes in white communities, REOs in communities of color are many times more likely to have multiple problems with respect to their physical condition, such as leaking roofs, broken windows, unsecured doors, trash in the yard, poorly maintained yards, and the like. They are less likely to be marketed effectively, are more likely to linger on the market longer, and are more likely to be bought by an investor rather than an owner occupant.[5] All of creates eyesores and hazards and depresses property values for the homeowners who remain.

In sum, the foreclosure crisis has had a significant impact on people and communities of color. For us at NFHA, addressing the sources of these problems and protecting against their recurrence have been a high priority, and one that we see as consistent with our civil rights mission. We were pleased when the OCC and the Federal Reserve announced their consent orders, and were hopeful that the effort to identify and compensate aggrieved borrowers would be an important step towards mitigating some of the damage done by servicers' abuses. We also hoped that the servicing provisions of the consent orders and the regulators' increased focus on servicing practices would result in better loss mitigation so that more borrowers would receive the loan modifications for which they were eligible and be able to stay in their homes.

Importance of the Independent Foreclosure Review and Consent Orders

The 2011 OCC/FRB consent orders, with their provisions requiring the servicers to conduct independent foreclosure reviews, were one of several efforts under way in recent years to address the foreclosure crisis. In 2009, Making Home Affordable was launched, with its HAMP, HARP, and Hardest Hit Funds programs. In February, 2012, 49 State attorneys general and several Federal agencies reached an agreement with five major mortgage servicers,[6] the National Mortgage Settlement (NMS). These efforts are aimed at preventing further foreclosures, by reforming mortgage servicing practices, standardizing loan modification terms and conditions, increasing the use of principal reduction in loan modifications, and making it possible for homeowners who were current on their mortgages but underwater to refinance into loans with lower interest rates. What sets the IFR apart from these other efforts is its emphasis on identifying and compensating borrowers who were harmed by problems in the way their servicer handled their mortgages and their requests for assistance when they could no longer make their payments.

This approach is particularly important from a civil rights perspective. As noted above, a disproportionate number of unsustainable subprime loans were made to African American and Latino borrowers. Many of these loans became unaffordable and unsustainable, forcing the borrowers into default, in the earliest waves of foreclosures. By the time the consent orders were signed, many of these borrowers may have already lost their homes. However, even if it was too late to help these borrowers save their homes, it was not too late to find them and compensate them, at least in part, for the harm they suffered. For this reason, NFHA has taken a particular interest in the implementation of the IFR process.

[4] Bocian, Debbie Gruenstein, Peter Smith, and Wei Li, "Collateral Damage: The Spillover Costs of Foreclosures", Center for Responsible Lending, October 24, 2012.

[5] National Fair Housing Alliance, "The Banks Are Back, Our Neighborhoods Are Not: Discrimination in the Maintenance and Marketing of REO Properties", April 4, 2012.

[6] The servicers covered by the National Mortgage Settlement include Bank of America, Citi, JPMorgan Chase, Wells Fargo, and GMAC/Ally (*see, www.nationalmortgagesettlement.org* for further details). All of these servicers also entered into consent orders with OCC and/or the Federal Reserve Board in April, 2011 and were subject to the requirements of the IFR.

Concerns With the Independent Foreclosure Review

The IFR had two components. One of these was the “look-back” process, for which the independent consultants (ICs) that the servicers were required to hire would review samples of files, and where a certain level of errors was found, expand those samples to capture all of the files of borrowers with similar characteristics. The second component was the Request for Review (RFR) process, which provided an opportunity for borrowers who believed they had been harmed to request a review of their particular file, whether or not it was also captured in one of the samples reviewed by the ICs.

Reviewing the files of 4.4 million borrowers who faced foreclosure to determine whether their servicers acted properly, whether the borrowers suffered financial harm, and quantifying that harm is a big, complex undertaking. For NFHA and the civil rights and consumer advocates with whom we work, it was important for the reviews to be:

- conducted in a timely and transparent manner,
- thorough while focusing in on the problems experienced most frequently by borrowers,
- fair and even-handed by capturing the borrower’s side of the story, and
- consistent, resulting in comparable outcomes for similarly situated borrowers with different servicers.

Transparency, consistency, and fairness have all proven problematic in the IFR process, as is evident in the record compiled by this Committee through its earlier hearings, and in the two reports published by the Government Accountability Office (GAO). With respect to the look-back process, NFHA and other advocates raised several key concerns.

Our first concern was the lack of transparency due to the regulators’ reluctance to make public the rulebook for this undertaking. Despite numerous requests, the regulators never released the guidance they provided the ICs about how to implement the reviews and how to resolve any issues that arose. This lack of transparency undermined public confidence in the process and made it difficult to have confidence that the ICs knew what to look for in the files or how to interpret what they found (or didn’t find). This lack of transparency also undermined public confidence that the outcomes would be consistent across servicers.

Further, the process did not allow for input from the borrower about his or her interactions with the servicer. This was necessary to identify cases where borrowers were given incorrect inconsistent or conflicting information by their servicers, and to shed light on the many instances in which borrowers submitted the documents required to be considered for a loan modification or other loss mitigation options—often several times—but servicers claimed never to have received them. For many borrowers, this had caused significant and costly delays in the processing of their loan modification applications. In some cases, the mounting arrearages made them ineligible for the modification they requested.

The Request for Review (RFR) process also raised many concerns. Again, the GAO report on the subject lays them out clearly. Many of these problems stemmed from the failure to provide for the kind of outreach necessary for the RFR process to be successful. This was a problem in the consent orders themselves. No resources were allocated for outreach; no organizations that work closely with borrowers, such as housing counseling agencies or legal services offices, were consulted about the best way to reach borrowers or what role they might play in doing so; no provisions were made for developing effective outreach materials; and no consideration was given to a reasonable timetable for such an effort.

A second, more targeted outreach effort was conducted during the last 6 weeks or so before the final application deadline. This resulted in a substantial increase in the number of borrowers who filed an RFR, but in the end only some 11 percent of eligible borrowers made such a request. Many borrowers may not have been in a position to submit an RFR, others may have lacked confidence that the outcome would justify the effort required, and a great many others may simply never have known that the IFR process existed and they could file a request to have their file reviewed. These are just a few of the concerns about the RFR process. Others were detailed in the testimony provided to this Committee by Alys Cohen, of the National Consumer Law Center, on December 13, 2011.[7]

[7] Cohen, Alys, “Helping Homeowners Harmed by Foreclosures: Ensuring Accountability and Transparency in the Foreclosure Reviews”, Testimony before the United States Senate Subcommittee on Housing, Transportation, and Community Development of the United States Senate Committee on Banking, Housing, and Urban Affairs, December 13, 2011.

Concerns With the January, 2013 IFR Settlement

On January 7, 2013, the regulators announced that they had reached a settlement with 13 of the IFR servicers, were halting the IFR process at those companies and replacing it with a combination of direct payments to borrowers and other forms of mortgage assistance. The settlement was valued at $9.3 billion, including $3.6 billion in direct payments to 4.2 million borrowers, and $5.7 billion in other assistance. The agencies expressed concern about the slow pace of the IFR process and the substantial cost of the Independent Consultants, already reported to be $2 billion, and stated their belief that the new settlement would put more money in the hands of more borrowers more quickly.

Questions About the Cash Distribution

Borrowers and their advocates certainly shared the regulators' frustration over the pace and cost of the reviews. Whether the new settlement provides a more equitable distribution of relief, however, is a different matter. Last week the regulators released a chart that details how payments will be allocated among 3.9 million borrowers (payment details have yet to be released for borrowers whose loans were serviced by Goldman Sachs and Morgan Stanley). They range from $300 to $125,000. At the top end of the scale, 2,041 borrowers will receive $125,000. These are borrowers who were protected under the provisions of the Servicemembers Civil Relief Act (SCRA), but whose servicers foreclosed on their homes anyway. Another 98 borrowers who were never in default but still lost their homes to foreclosure will also receive $125,000. At the bottom end of the scale, 2,358,441 borrowers whose servicers brought foreclosure actions against them after approving their request for a loan modification, whose servicers never reached out to them to offer assistance, or who fall into an "other" category will receive $300 apiece. None of these borrowers filed an RFR. Their 260,623 counterparts in the same categories who did file an RFR will receive either $500 or $600.

The chart raises more questions than answers. For example, it is not clear why responsibility for "slotting" borrowers into specific categories was given to the servicers and why their record systems, which are known to be seriously flawed, were used as the basis for the slotting process. Nor is it clear why certain categories of borrowers were awarded one amount of money and other categories were awarded a different amount. In the end, no determinations were made about which borrowers experienced financial harm. With the exception of the SCRA violations and the borrowers who were never in default, the fact that a borrower falls into a category higher on the chart is no indication that he or she actually experienced harm. Similarly, the fact that a borrower is slotted into a category lower on the chart is no indication that he or she did not experience harm. Given this, it is not clear why there are so many different categories of borrowers and awards, or even any categories at all. And given the likelihood that a great many borrowers never knew about the IFR at all, let alone that they could file a request for review, and the fact that no borrowers knew that doing so would affect the amount of compensation they would receive, it is not clear why borrowers who filed an RFR were awarded so much more compensation than their counterparts who did not file such a request.

These questions are confusing and distressing to borrowers, and I suspect many of the Members of this Committee are hearing from your constituents with these and other concerns about how this process has played out.

Advocates have many concerns about the payment process itself. As with the initial RFR process, no resources were allocated for outreach to borrowers to let them know about the change in plans and the fact that checks will be coming their way. Postcards from the payment agent, Rust Consulting, were mailed to borrowers, but these postcards are subject to the same critiques that GAO cited in its report on the previous IFR outreach process. We are already hearing reports that borrowers are confused about the postcards, believe they may come from scam artists, or are simply throwing them out as junk mail.

This, in turn, raises concerns about whether, when the IFR checks are mailed, borrowers will actually open the letters and cash the checks. It is critical for the regulators to track returned mail and cashed checks to determine whether the funds are not getting through in certain geographic areas or to groups of borrowers, particularly those who may not be proficient in English and may not fully understand the letter of explanation accompanying the checks. Despite advocates' recommendation, the regulators did not send postcards or letters in both English and Spanish, let alone any other languages. If gaps are identified among those borrowers cashing the checks, the regulators should take additional steps to ensure that they have the correct address for borrowers. They should also conduct additional, and where appropriate language specific, outreach in those communities to ensure that borrowers actually receive the funds to which they are entitled.

In addition, it is inevitable that some funds will go unclaimed. The regulators have not announced what will be done with such funds. After every effort is made to locate those borrowers who did not cash their checks and encourage them to do so, we recommend that remaining funds be earmarked to support housing counseling, legal services and other foreclosure prevention services.

Questions About the Other Forms of Assistance to Borrowers

There are also many questions and concerns about the provisions of the settlement relating to nonmonetary assistance to borrowers, the so-called soft dollar side of the settlement. The $5.7 billion worth of assistance will be provided to borrowers in the form of loan modifications, short sales, deficiency waivers and the like. The servicers themselves will determine which borrowers will receive assistance, how much, and in what form. The structure of this side of the settlement resembles the structure of the National Mortgage Settlement (NMS), in that servicers will receive credit towards their targeted level of borrower assistance for the specified activities.

There are some significant differences between the IFR settlement and the NMS, however, and many of these are cause for concern because they undermine the regulators' stated goal for this part of the settlement, which is to help save people's homes.

Our greatest concern is that, unlike the NMS, the IFR settlement bases the amount of credit the servicer receives on the unpaid balance of the loan, rather than the amount of assistance provided to the borrower. In other words, if a servicer forgives $50,000 worth of principal on a $500,000 loan, it receives soft dollar credit not for $50,000 but for $500,000. This severely inflates the amount of credit the servicer receives, and dramatically reduces the number of borrowers who are likely to receive assistance through this program.

An equally alarming aspect of this approach is that it creates an incentive for servicers to focus their efforts on higher-priced homes with larger unpaid loan balances. On a loan with an unpaid principal balance of $500,000, a loan modification that provides any amount of principal reduction—be that $1,000, $10,000, or $100,000—will yield $500,000 worth of credit for the servicer. A modification that provides the same amount of principal reduction on a loan with an unpaid principal balance of $150,000 will only yield $150,000 worth of credit.

This crediting structure encourages servicers to focus their efforts on large-balance loans. It is likely to disadvantage borrowers in communities of color, where home prices and therefore loan balances are systematically lower than those of comparable homes in predominantly white communities. Thus a process that initially held promise for remediating some of harm suffered by borrowers in communities of color may instead leave those borrowers out in the cold.

In another contrast to the NMS, the IFR settlement places loan modifications which have the real potential to save the borrower's home—on equal footing with short sales, in which the borrower loses the home. Both receive dollar for dollar credit under the IFR settlement. Unlike the NMS, the IFR settlement places no cap on the amount of credit that servicers can receive for short sales, so if they choose, servicers can meet their entire soft-dollar goals through short sales. Nor does the IFR settlement make any provision for resources to support outreach to borrowers and counseling or legal assistance. Funding for these efforts, which is strictly left to the discretion of individual servicers, will come out of the soft-dollar side of the settlement.

Ways in Which the IFR Settlement Could Still Be Helpful

The results of the 2011 consent orders and the IFR process to date have been extremely disappointing. They have failed to identify borrowers who were harmed by the actions or inactions of their servicers, and the checks that are being sent to borrowers will not adequately compensate those who were harmed. Nonetheless, the orders still provide the regulators with two key opportunities to help keep borrowers in their homes, if they choose to use them. These are through reforming servicing practices and ensuring that help goes to those borrowers and communities that have been hardest hit.

Servicing Reforms Needed

Servicing abuses remain widespread, and too often, servicers still are not providing borrowers with the loan modifications for which they are eligible. This is a problem that the 2011 consent orders were intended to fix, although this component of the orders has received little attention from the regulators, who have been focused on the IFR. While the regulators report that more than half of the more than 4 million homeowners who were in scope for the IFR process have subsequently lost their homes to foreclosure, as many as two million have not. For these and other at-risk homeowners, it is critical that the regulators step up their focus on loss mitigation and servicing reforms.

In addition to the servicing reforms spelled out in the consent orders, the regulators have broad supervisory authority to ensure that servicers comply with other contractual and programmatic requirements. If the regulators were to put more emphasis on servicing reforms in their compliance reviews, borrowers would benefit tremendously. To do this, they must bring their examination teams up to speed on what servicers should be doing, and get input from the field about how servicers are actually performing.

The ongoing servicing problems are illustrated by a survey of housing counselors in California, released earlier this month by the California Reinvestment Coalition.[8] The survey focused on the provisions of the NMS and the servicers to which it applies, but the results are indicative of more widespread problems in the industry. Seventy percent of the counselors who responded to the survey reported that the single point of contact provided to borrowers by their servicer to manage and assist in their request for a loan modification was never, rarely, or only sometimes accessible, consistent or knowledgeable. More than 60 percent of counselors reported that the servicers always, often or sometimes pursue foreclosure while the borrower is still under review for a loan modification. Sixty percent or more of counselors reported that servicers never or rarely make decisions about loan modifications within 30 days of receiving a completed modification, and a majority of counselors reported that servicers rarely or never acknowledge receipt of applications in a timely manner or notify borrowers of documents needed to complete their applications. Counselors also reported problems with servicers giving borrowers enough time to supply missing documents, losing documents, and improperly denying loan modifications to borrowers who appear to be qualified for them.

Through aggressive use of their authority under the provisions of the consent orders, as well as their broader supervisory authority, the OCC and the Federal Reserve could help to bring about much-needed changes in servicing practices and help homeowners keep their homes. Advocates have recommended that the regulators take some specific steps to accomplish this:

1. The regulators should increase their oversight of loss mitigation practices and the servicers' compliance with contract, regulatory, and programmatic standards.
2. The regulators should require those servicers covered by the consent orders to certify that they have properly reviewed borrowers for loan modifications or other loss mitigation options before moving forward with any action that results in the loss of a home.
3. The regulators should establish a separate appeals or complaint process for IFR borrowers who believe their servicer has acted improperly, and inform those borrowers of this channel for an outside review of their case. Foreclosures should be halted until any such complaints are resolved.
4. In cases where servicers consistently break the rules, the regulators should impose significant penalties.

These four steps could make a big difference for millions of homeowners seeking to stay in their homes.

Ensuring That Help Goes to Those Most in Need

While the consent orders and recent settlement agreements provide the regulators with few tools to ensure that help goes to those most in need, they do allow for the regulators to collect detailed information on the actions that servicers take to meet their soft-dollar crediting targets. Servicers will submit reports to the regulators every 45 days. The regulators should make this information available to the public at a granular level to establish some accountability for the servicers.

Advocates have recommended that the regulators collect and disclose the detailed information by servicer and census tract. The data collected should include, at a minimum:

- the number of borrowers still in their homes,
- the number who have applied for loan modifications,
- the number of modifications approved for both first and second liens (linked where possible),

[8] California Reinvestment Coalition, "Chasm Between Words and Deeds IX: Bank Violations Hurt Hardest Hit Communities", April, 2013. Available at *www.calreinvest.org/*.

- the terms of the modification (interest rate reduction, principal reduction, change in payment amount, etc.),
- the number of modifications denied and the reasons for denial,
- the number and dollar value of short sales, deeds in lieu of foreclosure, and associated deficiency waivers, and
- the dollars allocated for housing counseling services.

It is critical for these data to be reported at the census tract level. This is the only way to determine whether the allocation of the IFR' s soft dollar assistance is going to communities most in need. The lack of such data under the NMS has been a major source of frustration for civil rights groups, community organizations and counseling/legal services agencies. Many of these groups report that their clients and constituents are not receiving offers of assistance under that settlement, and wonder where the help is going. The OCC and Federal Reserve have the opportunity to do a better job of tracking the funds, and we hope Congress will encourage them to do so.

Conclusion

Congress has a crucial role to play in making sure that the Federal regulatory agencies responsible for policing the Nation's mortgage market do their jobs. Unfortunately, we are not yet at the point where either Congress or the public can have confidence that mortgage servicers are in compliance with their obligations under various enforcement actions, program guidelines or their contractual with their investors. The problems are widespread and long-lasting, with millions of homeowners still at risk of foreclosure, it is important that servicers correct these problems in order to prevent unnecessary foreclosures and speed our economic recovery.

Looking ahead, NFHA is concerned about gaps in the existing servicing standards and those that will go into effect next year. Among other things, these gaps leave borrowers with disabilities, those with limited English proficiency, and the widows and heirs of deceased borrowers without the protections they need to get the help they deserve from their mortgage servicers. We look forward to working with you to address these gaps in the servicing standards and to make it possible for the greatest possible number of vulnerable borrowers to keep their homes.

Thank you for the opportunity to testify here today, and for your ongoing oversight of the Independent Foreclosure Review process. I will be happy to answer any questions you may have.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR REED FROM DAVID HOLLAND

Q.1. How closely did the OCC and the Federal Reserve monitor and oversee your participation in and your duties with respect to the IFR settlement? How often and in what manner?

A.1. The Federal Banking Regulators participated in and monitored key decisions and elements of the Settlement process. This included but was not limited to matters of:

- Structuring of the Qualified Settlement Fund Entities and bank accounts.
- How settlement funds were deposited.
- Coordination of borrower loan classification on behalf of the Servicers.
- Reconciliation of the data loan classifications between Rust, the Servicers, and the Regulators.
- Review and approval of all correspondence.
- Review and approval of call center scripting.
- Review and approval of Web site content.
- Review and approval of letter and check mailing schedules.
- In-person, on-site review of the end-to-end process the print vendor implemented for print production, and the quality check steps incorporated throughout the printing process.
- During the early stages of the Settlement, the OCC was on-site at Rust for the purposes of gathering information and exploring settlement administrative options. Subsequently, Rust had weekly planning sessions with the OCC to discuss the implementation and production schedules. These planning sessions were conducted via teleconference, and decisions were documented in an End-to-End Implementation Plan. The Rust IFR Payment Agreement Processes were also reviewed and documented. As we moved closer to the initial check mailing date, a second weekly meeting was added to ensure all the necessary items were addressed and considered leading up to the check mailings.
- Once checks were mailed, daily conference calls were established which included the OCC, FRB, Rust, and Huntington National Bank. These daily calls reviewed operational performance, issues logs, check clearing status and future processes.

Q.2. What procedures did you have in place to ensure checks did not bounce?

A.2. We believe it is important to first clarify that a "bounced" check is intrinsically different than a situation in which a check-cashing store or other financial institution declines to cash a check. Huntington Bank has indicated that no valid checks were returned for insufficient funds (bounced). However, a small number of checks were not honored at the point of cashing for reasons detailed in this response.

Rust was responsible for working with OCC and Federal Reserve to:

- Execute advance notification to borrowers.

- Establish a schedule for payment waves.
- Arrange for servicer deposits of funds at Huntington National Bank.
- Establish and staff toll-free phone numbers for borrowers to call with questions and for financial institutions to call to verify checks and funds availability.
- Print and mail checks.
- Review Huntington National Bank's prepared reports for fraud attempts.
- Rust also implemented the additional safeguard of printing a toll-free number on the back of checks to assist borrowers and financial institutions with check processing.

At Rust's recommendation, Huntington National Bank of Ohio was selected by the OCC and Federal Reserve as the financial institution in which settlement funds would be deposited and that would process and clear the settlement checks.

Rust sent postcards to the 4.2 million borrowers notifying them in advance of their eligibility to receive payment under the agreement.

Funds for payment were deposited with Huntington National Bank by the 13 servicers at various times on or before April 5, 2013. The first wave of check was mailed on April 12, 2013.

A collaborative decision was made by the regulators, Huntington Bank and Rust, that checks were to be cleared through a "zero balance" account in Huntington National Bank. In a "zero balance account", checks are paid without holding excess funds in a checking account. All interest earned on the funds accrues to the benefit of the fund.

To assist borrowers and to mitigate opportunities for fraud, Rust Consulting printed a toll-free number on the back side of each check to allow check-cashing stores and other financial institutions to call Rust and validate the check. Through April 25, 2013, more than 44,000 callers to this number had spoken with a Rust customer service representative. Through April 24, 2013, we have identified thirty-two (32) fraudulent checks submitted as settlement payments. Huntington National Bank, in its role as the issuing bank, initiated an Early Warning Service for the payments on April 16, 2013, four days after the first wave of checks were mailed.

Q.3. Have you addressed your flaws in internal controls and procedures that led to this unfortunate outcome?

A.3. Response:

- Huntington National Bank instituted the Early Warning System on April 16, 2013.
- Huntington National Bank removed the zero balance account structure so that Huntington National Bank tellers would no longer see a zero balance when accessing the checking account.
- We have determined that when some check stores called to validate checks, they also asked Rust Consulting to guarantee that adequate funds were available, which only a bank representative can do. In response, we established a process to

link callers to Huntington National Bank for the necessary guarantee.

- As of April 25, 2013, almost 1.1 million settlement checks worth over $1 billion have cleared.
- We continue to work with Huntington National Bank and borrowers to ensure that future payments can be negotiated without unnecessary delay.

Q.4. In light of this setback, would you agree to have your fees withheld until all payments are satisfactorily delivered to their intended recipients? If not, what protections are currently in your contract that ensure that these sorts of mistakes do not happen again?

A.4. Response:

- While we have been disappointed to learn that a relatively small number of check recipients encountered problems when they tried to cash their checks, we are also very proud of the assistance that we have provided to thousands of recipients whose checks were validated via our toll-free number for financial institutions.
- We have addressed check-processing issues with Huntington National Bank, in their role as the check-issuing institution, and they have assured us that appropriate banking procedures and market notifications are now in place to prevent a recurrence of issues experienced by a relatively small number of borrowers in the first wave of checks.
- Working with the OCC, Rust has developed extensive processes and procedures to ensure a smooth and error free plan of administration. We believe to date the plan has been executed by Rust and the results to date have been favorable.
- We have individual contracts with the 13 servicers. Our contracts generally focus on defining our arrangements, scope of work and liability with regard to errors that result in a financial loss.
- We do not believe a delay in payment of Rust Consulting's fees is warranted.

Akin Gump
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May 14, 2013

VIA HAND DELIVERY

Mr. James Ahn
Office of Senator Jack Reed
Committee on Banking, Housing and Urban Affairs
United States Senate
Dirksen Senate Office Building, SD-534
Washington, DC 20510

Re: Rust Consulting, Inc.

Dear James:

On behalf of our client, Rust Consulting, Inc. ("Rust"), we appreciate the opportunity to supplement our responses to the Committee's Questions for the Record by providing an update on the Independent Foreclosure Review ("IFR") settlement payment process. Attached here is a White Paper that lays out in careful detail the facts about the program and the events surrounding the various settlement payments. In addition to a general overview about the IFR program, challenges inherent in such a large program and background about Rust, we've also included a point-by-point analysis of the factual errors contained in the May 8, 2013 *New York Times* article. The enclosed information represents our current understanding with respect to the issues raised in that article. We are continuing to look into any issues that have arisen in the implementation of this large settlement process

If you have any questions or comments, please do not hesitate to contact me at any time. We look forward to continuing to work with the Committee in a cooperative manner. Please let us know if you have any questions.

Sincerely,

Steven R. Ross
Counsel for Rust Consulting, Inc.

Enclosure

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Independent Foreclosure Review Settlement Payments

Background, Process and Status – from Rust Consulting

What is the IFR?

The Independent Foreclosure Review (IFR) settlement is a massive and complex undertaking. It results from an agreement reached in January of 2013 between 13 separate mortgage-service companies and federal banking regulators. The servicers agreed to pay a combined $3.6 billion to 4.2 million borrowers whose primary residence was affected by a foreclosure process in 2009 or 2010 by one of these servicers.

Federal banking regulators and the 13 mortgage servicers negotiated the $3.6 billion amount to be paid to borrowers. Contrary to certain inaccurate news articles, Rust Consulting was not part of these decisions.

Rust was selected as the "Paying Agent" to administer the predetermined settlement payments to eligible borrowers. The mortgage servicers gave Rust the names and last-known addresses of the 4.2 million borrowers as well as the payment category for each borrower. Federal banking regulators validated the process by which servicers categorized borrowers and determined the amount of payment that would be paid to borrowers in each category.

Who is Rust Consulting?

Rust Consulting has provided administration services for complex projects for more than 30 years. In that time, the company has handled over 3,500 projects similar in nature to the IFR Payment Agreement. The company's key strengths include claims processing and adjudication, payment distribution, tax reporting, data management and security, all types of notification and claim forms support,

Key Points:

- No IFR settlement checks were returned for insufficient funds. Initially, a very small number of check-cashing stores and banks declined to cash checks. Rust assisted the processing bank, which worked quickly to resolve issues the check-cashing stores and banks were having.
- Payments with an incorrect amount went to 96,000 borrowers in the May 3, 2013, mailing. A clerical error occurred in which payment amounts were pulled from the wrong data table. Affected borrowers will receive a supplemental check for the balance due.
- The 13 separate mortgage servicers gave Rust the names, addresses and categories for borrowers.
- Federal banking regulators validated borrower payment categories and determined how much borrowers in each category would be paid.
- Rust's role is to administer and distribute the predetermined payments.
- Rust earns no interest on these settlement funds or uncashed checks.
- Rust maintains a borrower customer care center that has handled 660,000 consumer calls to date. The center can be reached at +1 (888) 952-9105.

regulatory compliance and customer contact centers.

Steps to Facilitate IFR Payments

Based on its experience, Rust anticipated that a program with the IFR's scope – with millions of participants, billions of dollars and recipient data from 13 separate sources -- inherently would present challenges in many individual cases. Rust took multiple steps to improve the process for eligible borrowers as well as financial institutions that would receive checks for cashing or deposit.

As an added measure to facilitate payments in such a large distribution, Rust had a toll-free number printed on the back of each check. The goal was to provide faster service for borrowers and to reduce fraud opportunities. Since the first wave of payments was mailed on April 12, 2013, this "teller line" has handled more than 100,000 calls from check-cashing stores and financial institutions.

In addition, Rust established two customer call centers in Minnesota to assist borrowers, employing approximately 1,100 customer service representatives. The centers are open for calls 14 hours every weekday and for 9 hours on Saturdays. To date, the centers have handled more than 660,000 borrower inquiries. Customers in need of assistance can call the center toll-free at +1 (888) 952-9105.

Settlement Funding and Payments

Funds were deposited by the mortgage servicers at the processing bank well before the first checks were mailed. Funds were readily available to cash checks. During the initial days after the first mailing, a very small number of instances occurred when a check-cashing store or bank declined to cash a settlement check. Rust assisted the processing bank, which worked quickly to resolve issues that check-cashing stores and banks were having. Based on reports it has received, Rust believes that nearly all borrowers who attempted to cash an IFR check were able to do so without any difficulty.

No check was returned for insufficient funds. In the first 17 days after the initial mailing, 1.2 million settlement checks worth more than $1.2 billion cleared the bank. As of Friday, May 10, 2013, more than 2.1 million borrowers have cashed or deposited settlement checks worth $1.9 billion.

Rust Earns No Interest from These Settlement Funds or Uncashed Checks

Rust administers payments to borrowers from the IFR settlement funds. Rust earns no interest from these settlement funds or uncashed checks.

Partial Payments to Certain Borrowers in May 3, 2013, Mailing

Payments with an incorrect amount went to 96,000 borrowers in the May 3, 2013, mailing. A clerical error, which Rust regrets, occurred in which payment amounts were pulled from the wrong data table. Upon learning of the error, Rust immediately began taking steps to issue supplemental checks to pay affected borrowers the remaining balance of their payment. This

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helps ensure that all borrowers receive the full payment amount, as determined by federal banking regulators.

Borrower Information Changes

Throughout this project, Rust has processed many thousands of address and name changes, updating the initial borrower information that in many cases was four years old when Rust received it. Rust conducted research to help ensure accurate updates as needed.

The company also maintains a dedicated "IFR triage team" that helps resolve issues such as changes in borrower status including new addresses, new names or the death of a borrower. To prevent fraud, each change request is reviewed and validated to help ensure that an authorized borrower is requesting the change.

When new information for borrowers is verified, reissued checks will be mailed in batches. The timing is subject to regulatory review.

Inaccurate Media Coverage

Recent stories published by the New York Times contained numerous factual errors and mischaracterizations of Rust and the IFR project. An analysis of the May 8, 2013, story follows:

***New York Times* Story**	**The Reality**
New York Times, May 8, 2013 **"Errors Afflict More Checks Issued to Aid Homeowners"**	
NYT: "At least these checks cleared. Three weeks after checks sent to homeowners as compensation for foreclosure abuses were rejected for insufficient funds, the consulting firm at the center of the mishap erred again: a fresh round of checks was written for the wrong amounts.	A very small number of check-cashing stores and banks declined to cash checks. Rust assisted the processing bank, which quickly resolved the issues that check-cashing stores and banks were having. The processing bank has indicated that no checks were returned for "insufficient funds." Funds were deposited by the servicers at the processing bank well before the first checks were mailed. Funds were readily available to cash checks.

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"In recent days, according to officials briefed on the matter, Rust Consulting issued nearly 100,000 checks for less than the homeowners were owed. The mistake potentially cheated consumers out of millions of dollars they were owed under a deal reached between the government and the nation's biggest banks.	The lower payment amounts resulted from an unintentional human clerical error. Rust is issuing supplemental checks that will be mailed as early as May 17, 2013, to pay affected borrowers the remaining balance of their payment.
NYT: "... the developments cast another harsh spotlight on Rust, which had been selected as the distributor of checks for the $3.6 billion settlement deal that regulators struck with the banks. The continued problems with Rust also raised questions about the government's oversight of the firm and the wisdom of hiring it in the first place.	To the contrary, Rust's experience with large and complex settlement distributions enables quick resolution of issues inherent in such a large and complex project.
"What's more, some homeowners complain the problem is broader than Rust has acknowledged. Jennifer Lawson, whose husband is on active duty with the Navy, said she was stunned when she received a check on April 19 for $600. Under the terms of the settlement deal, Ms. Lawson expected thousands of dollars in compensation for her foreclosure...	The article thoroughly mischaracterizes the entire IFR process and Rust's role in it. Rust had no input into determining what amount of payment borrowers would receive. Mortgage servicers provided names and last-known addresses as well as the categorization of borrowers. Regulators validated the process by which servicers placed borrowers into payment categories and determined payment amounts for each category. Rust is implementing the predetermined decisions, and administering payment and customer contact centers.
NYT: "But problems emerged soon after the settlement was announced in January. The consulting firm, officials said, was initially slow to alert borrowers to expected payments. Then, the officials say, Rust delayed the checks for weeks as it struggled to gear up for the payments. Once Rust issued the first round of checks in April, it failed to move money into the bank account used for the settlement. The	Rust worked with federal banking regulators to distribute the checks in a timely fashion. Funds were deposited by the mortgage servicers at the processing bank well before the first checks were mailed. Funds were readily available to cash checks. Rust printed a toll-free number on the back of

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decision prevented some homeowners from cashing their checks…	checks to facilitate the process for borrowers. Rust assisted the processing bank, which quickly resolved the issues that check-cashing stores and banks were having. In just 17 days after the first wave of checks were mailed, 1.2 million checks worth more than $1.2 billion had cleared.
NYT: "But, in effect, the checks bounced. And after the incident, Rust lost significant credibility with the regulators, officials said.	
"More recently, homeowners have complained about clerical errors at Rust, problems like checks sent to the wrong addresses or issued to deceased borrowers.	The article mentioned individuals who experienced life changes (new name, address, etc.), which affected their ability to receive or process their check. Rust is sympathetic to these individuals and is working with borrowers on information changes. To prevent fraud, each change request is reviewed and validated to help ensure that an authorized borrower is requesting the change. Reissued checks will be mailed in batches. The timing is subject to regulatory review. Rust's borrower call center is open for 14 hours Monday through Friday and for 9 hours on Saturday to assist borrowers with information and change requests. We also have a dedicated "triage team" to address needs.
"The firm's latest mistake — sending out checks in the wrong amounts — could also prove difficult to remedy.	The remedy was instituted quickly once the error was identified, and supplemental checks for the balance due to affected borrowers will be mailed out as early as May 17, 2013.
"The problem stems from last week, when Rust issued checks to customers of Morgan Stanley and Goldman Sachs… "But Rust, according to the officials briefed on the matter, failed to follow the payout plan. Instead, it issued checks to customers of Goldman Sachs and Morgan Stanley based on a metric adopted by the 11 other banks, including JPMorgan Chase and Bank of America.	Rust regrets that payments with an incorrect amount went to 96,000 borrowers in the May 3, 2013, mailing. A clerical error occurred in which payment amounts were pulled from the wrong data table.

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"The misstep deprived some homeowners of thousands of dollars. For example, some Goldman and Morgan customers in bankruptcy who were wrongfully evicted deserved a $4,650 check. They received $3,750 instead…	All borrowers who received less than they should are being issued supplemental checks that will be mailed as early as May 17, 2013 to pay affected borrowers the remaining balance of their payment.
NYT: "Rather than cancel the checks, Rust decided to issue a second round of payments to the harmed consumers. In a statement, the Fed instructed borrowers to "cash both the original checks and the supplemental check." It also noted that "Rust has determined that the error was limited to borrowers whose mortgages were serviced by Goldman Sachs and Morgan Stanley."	Canceling checks would have created massive confusion among borrowers as well as financial institutions and also would have opened new avenues for fraud.
"But anecdotal evidence suggested that Rust had encountered separate problems, beyond Goldman and Morgan. Housing advocates point to the case of Ms. Lawson. Under a federal law, banks are required to obtain court orders before foreclosing on active-– - duty members like Ms. Lawson's husband. Some military members who were wrongfully evicted are eligible to receive up to $125,000 in compensation through the settlement. Ms. Lawson, whose home near Jacksonville, Fla., was sold at a foreclosure auction in 2010, said the "piddling amount" of $600 was an injustice.	Rust sincerely sympathizes with this family as well as the millions of other individual experiences that led to the IFR process. Rust's role is solely to distribute settlement funds to eligible borrowers. The mortgage servicers placed borrowers into payment categories. Federal banking regulators validated the process by which servicers placed borrowers into payment categories and determined payment amounts for each category.
"Mr. Cummings, the congressman from Maryland, also notes that Rust does not include an explanation of what homeowners are owed under the settlement…	Information that Rust can provide to borrowers is determined collaboratively with regulators.
NYT: "Regulators have noted that many consumers have seemingly had no trouble cashing their checks. By the end of Tuesday, regulators say, homeowners successfully cashed or deposited about two million checks, or slightly more	

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than half of the total checks issued.	
"Still, that leaves nearly two million people who have either delayed cashing the check or have had problems doing so...	The 4.2 million checks are being mailed in waves that began on April 12, 2013. The most recent wave went out May 3, 2013. In projects of this nature, it is not unusual for check recipients to hold their checks for some period of time. Rust has resolved known issues. Except for individual cases that require additional attention, borrowers are able to cash or deposit their checks upon receipt.
NYT: "One of Ms. Singerman's clients whose home in Pleasanton, Calif., is in foreclosure cannot cash the $1,000 check she received from Rust in April. The problem, Ms. Singerman said, is that the check is made out to the homeowner's husband, who died more than three years ago.	Rust has appropriate processes in place for updating records and makes updates on a daily basis. The necessity to prevent fraud requires verification before a check can be approved for reissue.
	Closing note: Rust does not earn any interest on these settlement funds or from checks that have been mailed but not deposited or cashed.

Rust urges any check recipient with an issue to call the company's borrower contact center at +1 (888) 952-9105.

The enclosed information represents our current understanding with respect to the issues raised in certain media. Rust continues to look into any issues that have arisen in the implementation of this large settlement process.